



ENTRE- PRENEURS

AND

INITIAL PUBLIC OFFERINGS

Decision – Process – Impact

**Jocelyn J.Y. Desroches
Vijay M. Jog**

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**ENTREPRENEURS AND
INITIAL PUBLIC OFFERINGS:
DECISION - PROCESS - IMPACT**

**A study of
owner-managers of small firms
listed on the Toronto or Montreal Stock Exchange**

and

**owner-managers of small unlisted firms
with stock market potential**

MONTREAL, 1991



**ENTREPRENEURS AND
INITIAL PUBLIC OFFERINGS:
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By

Jocelyn J.-Y. Desroches

and

Vijay M. Jog

with collaboration from

Ghislain F. Théberge

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AUTHORS

DESROCHES, Jocelyn, J.-Y.

B.A., Lic. es. Ed. Sc., M.A., M.B.A., Ph.D. (Toronto)

- Professor in Management
- Head of Management Division
- Associate Director of the Department of Administrative Sciences
Université du Québec à Montréal

JOG, Vijay, M.

B.Eng., M.Eng., M.B.A., Ph.D. (McGill)

- Professor in Finance
Faculty of Business Administration
Carleton University (Ottawa)

THEBERGE, Ghislain, F.

B.A., B.Sc. Soc., M. Sc. Soc., M.P.A. (Université du Québec)

- Invited Professor in Small Business Management
Faculty of Administrative Sciences
Université Laval
- Lecturer in Management
Department of Administrative Sciences
Université du Québec à Montréal
- President, Les Matériaux de pointe PRECITECH Inc.
Québec (Québec)

**With the
Participation of**

Julien Naud
B.A., M.A., M.B.A. (Laval)

Professor in Management
Université du Québec à Trois-Rivières

and

President, Firme Grapho Laser Enr. Québec (Québec)

and

Head of IDE Management Research Group, Québec (Québec)

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Mr. Bruno Riverin, President

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Original listings
Mr. Rob Cook, Director
Mr. Pearce Bunting, President



FOREWORD

The role of small and medium-sized businesses in today's economy is wellknown. However, support measures are a relatively recent phenomenon whose effects have not yet been studied in any depth. So the question may be asked: have the efforts of government in Quebec and the other provinces, in particular as far as the QSSP and equivalent programs are concerned, really lived up to expectations in terms of countering small business capitalization problems?

The authors of this study, in an attempt to provide a preliminary answer to this ambitious question, carried out their research among owner-managers of listed SMBs. Their intention was to measure the effects of the QSSP on entrepreneurs, firms and individual firms' environments. From the research emerged a profile of SMB owner-managers who were open to the idea of stock market financing, compared to those who had rejected the idea. It also highlighted the effects of stock market listing on enterprise management: introduction of a structured information system, more rational administration and longer-term vision. Finally, it showed how much the perception of firms having chosen to go public improved in the eyes of their environment: they tended to enjoy a new prestige in the business world and investors had more confidence, which in turn meant easier access to other types of funding.

The research was carried out among SMBs listed on the Montreal or Toronto Stock Exchanges, which meant that SMBs in Quebec could be compared to those from other provinces, in particular Ontario. Some small differences were identified.

While entrepreneurs considered that Quebec's SSP, and similar programs in other provinces, had their good points, nevertheless some difficulties were mentioned, in particular with respect to information. Government people responsible for small business programs could therefore use the results of this research and the comments of entrepreneurs involved in it to improve access to the QSSP and other programs, and stock market institutions could also provide more and clearer information on their admission criteria.

This document will also be of interest to heads of small firms considering the public stock option. It provides a mine of information on the impact of going public - as perceived by the entrepreneurs themselves - and may well also help reduce owner-managers' justified and less rational fears with respect to the stock market. That is the main reason for the involvement of the Institute for Research on Public Policy's Small Business Program in this research. The study was the first of its kind in terms of scope, and should provide a model for similar research in other countries where government wish to encourage the development of small business. The results also provide some interesting comparative elements.

ROD DOBELL
President.

July 1991.

THANKS

Starting to write a book is one thing - but finishing it is something else entirely! Today, some four years after Ghislain Théberge's «intuition», and thanks to encouragement from Yvon Gasse, Director of the Institute for Research on Public Policy's (IRPP) Small Business Section, and his advisory committee led by Roger Blais, professor and researcher at the Université de Montréal's Polytechnique, we are both proud and delighted to dedicate this research report to everyone who was involved in any way - and especially to the hundreds of entrepreneurs who took part in the study.

The special skills and sustained efforts of Ghislain Théberge and Julien Naud meant that they were key elements in the initiation and design of the project, the formulation and validation of questionnaires, the choice of research populations and samples, data gathering and preliminary analysis of the results. Their contribution, together with help received from Ahmed Naciri, professor and researcher in the Department of Accounting at the Université du Québec à Montréal (UQAM), enabled UQAM's Management Research Centre to publish five working papers describing the research orientations and general conclusions from a preliminary data analysis.

Raymond Trémolières, professor and researcher with the Institute of Business Administration at the Université d'Aix-Marseille, also made his mark on the research through his participation in a comparative analysis of entrepreneur personalities in the four samples, and through his enlightened and judicious advice on the planning and preparation of the manuscript in its final stages.

Raymond Théorêt, professor of finance in the department of administrative sciences at the UQAM, has also provided us with strong moral support, encouragement and expert advices throughout the study.

The contributions of committed and enthusiastic research assistants - Dorothée Dawson and Larbi Hammami - as well as by Catherine Watson, André Hains and Raymond Laliberté, all three research professionals with, respectively, McGill University, the weekly magazine *Les Affaires* and more recently with the Radio Network Telemedia Communications, and UQAM's Management Research Centre, were important factors at many stages of the research.

Francine Lacasse, Nathalie Hénault and Diane Lemay, secretaries with UQAM's Department of Administrative Sciences, were, at various stages, all involved in typing and presenting the document. However, the final document was produced by Diane Lemay with great diligence, professionalism and a meticulous concern for excellence. Marko Beauchesne, Patrice Derome, students at UQAM's undergraduate business management program, and Frédéric Lannoye, a student at H.E.C. (Hautes Études Commerciales), produced the many high-quality diagrams. Christine Gardner, translated and adapted the manuscript into English from French with accuracy and perspicacity. We are very grateful to her for her most professional work.

The national scope of the project and the analytical depth were both made possible by the professional encouragement and financial support of the Institute for Research on Public Policy, the main funding organization, and the Montreal and Toronto Stock Exchanges, which provided secondary funding. The following contributions are worthy of special mention: Mr. Yvon Gasse, of the IRPP; Robert Lavallière, Richard Morin and Raphaël Gonzalez, each responsible in turn for the Enterprise Service Division of the Montreal Stock Exchange, later known as the Market Development Division, and Mr. Guy Bérard, Communications Vice-President in 1987 and now Vice-President of the Paris Stock Exchange, for having believed in the project and convinced the Montreal Stock Exchange's top people of its worth; and Marie-Josée Larocque and Jennine Ballard of the Toronto Stock Exchange. The financial support received from their organization, together with their personal open-mindedness, meant that the research could take on a pan-Canadian dimension.

Grants from our main sponsors also meant that substantial additional funding could be obtained from the Fonds pour la Formation des Chercheurs et l'Aide à la Recherche (FCAR) and the Social Sciences and Humanities Research Council of Canada (SSHRC). These two funding bodies play a vital role in Quebec (in the case of FCAR) and Canada (in the case of SSHRC) and made a significant contribution to this multi-disciplinary and multi-institutional research project.

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Any errors of fact or interpretation that may have slipped into the final document, despite considerable efforts to eliminate them, remain the responsibility of the authors.

JOCELYN J.-Y. DESROCHES, Ph.D.
VIJAY M. JOG, Ph.D.

July 1991.

SYNOPSIS

THE AIM OF THE RESEARCH

The aim of this research was to identify the reasons leading small business owner-managers to choose stock-type public funding, and to assess the effects of their choice on both themselves and their firm.

POPULATION

The research compared two groups of small firms¹:

- listed firms;
- unlisted firms with the potential to go public, in two geographically and culturally different regions: Quebec and Ontario.

In this latter group, some owner-managers were already considering the possibility of going public, while others had rejected the idea.

¹ The term "small firm" means that the small Quebec-based firms making up the sample had tangible assets of \$15 000 000 or less at the time the research was carried out. For firms in the est of Canada, this maximum limit had to be extended to \$20 000 000 in order to validate certain hypotheses.

COMPARATIVE THEMES

1. The physical attributes of the firms themselves;
2. The factors affecting the decision to go public or not:
 - factors related to the entrepreneur
 - factors related to the firm
 - factors related to the environment;
3. The impact of public funding on entrepreneur valorization both inside and outside the firm;
4. The role of the State in the decision process.

TARGET READERS

1. Entrepreneurs and their employees;
2. Stock exchange managers and brokers;
3. Legislators and civil servants responsible for programs and policies in the field;
4. Experts or anyone else interested in entrepreneurship, the decision process and behaviour of owner-managers of growing small firms.

Chapter 1

SMALL AND MEDIUM-SIZED BUSINESSES (SMBs) AND PUBLIC FINANCING: INTRODUCTION

1.0 Introduction

Small and medium-sized firms (SMBS) are increasingly being recognized as the driving force of the economy. Their capacity to innovate, their flexibility in adjusting to technology and their ability to adapt to current needs has led them to become the most important net job creators "... in Quebec, in Canada, in America and around the world" (Tardif, 1985: 1) (See also Bourassa, 1984: 10; Smith, 1984: 4; Bulloch, 1985). Small wonder, then, that governments attach so much importance to their development.

During the last thirty years, the Government of Quebec, like the governments of the other Canadian provinces, introduced various initiatives to foster the emergence and growth of small- and medium-sized firms. Other than programs to encourage venture creation, most such initiatives offered direct assistance to entrepreneurs through management improvements, equipment and real estate purchases and increased profitability. Other programs were introduced to foster public investment; from the end of the 1970s up to the stock market "crash" of October 1987, they had a decisive impact on both firms and investing individuals. Two points can be made here.

This research has revealed that, according to 70% of Quebec's entrepreneurs involved and 89% of those from other Canadian provinces, public financing is, for growing SMBs, "the best way of obtaining additional capital". The experts from the Commission québécoise sur la capitalisation des entreprises describe the first public issue as the critical stage in the development of a small firm's capital structure after business start-up and the first time outside owners and funds are brought into the firm (1984: 63).

In addition to meeting the capital and equity needs of SMBs, the Quebec Stock Savings Program (QSSP) introduced by the Quebec government also provided small investors with a new kind of investment in the more promising economic sectors: small and medium-

sized businesses. When this research began, in the summer of 1987, and even in the preceding years, the QSSP had become the most popular government program among business people and average investors. Martin considers it to be "the program that has registered the highest increase in participation by Quebec's savers since it was created" (1988: 12).

However, after the October 1987 stock market crash, stock market financing dried up and has never really recovered. In 1990, three years later, is the QSSP program for small business financing still viable? ... And if so, under what conditions?

This research was intended to identify the reasons and interests of entrepreneurs using this type of financing, and the impact it had on them and on their firms. To a certain extent, it aims to assess the impact of the QSSP phenomenon on entrepreneurship in Quebec and the extent to which public financing has helped the growth process of Canadian SMBs.

1.1 Research objectives

The objectives of this research were, first, to achieve a better understanding of the phenomenon of public financing and, second, to determine how SMBs could be encouraged to take more interest in it.

1.1.1 *The phenomenon of public financing*

There were a number of questions to be answered with respect to public financing. They are, in order:

1. At the time the decision is made, what were the influential factors and the decisional processes that led the heads of SMBs to use public financing?

The main points to be examined were:

- What characteristics distinguish the individuals and firms that choose public financing?
 - What factors influence the decision of a entrepreneur-owner to use stock market financing?
 - What is the relative importance of personal factors (i.e. those linked to the owner's personality) as opposed to factors (both internal and external) related to management of the firm?
2. In terms of the stock exchange listing process, how well-prepared were owner-managers when their firms were first listed on the stock exchange? The following specific questions were posed:

- How much did entrepreneurs know about the conditions governing eligibility and the procedures to be followed for a first public stock issue?
 - How did small business owners experience the period between their decision to go public and the time their firms were first listed?
 - What improvements would firms having gone through this experience suggest?
3. During the period immediately following stock exchange listing, what were the consequences of public financing for both entrepreneurs and their firms?

In particular,

- What impact did public financing have on: the firm's status, its management and the owner himself?

All these questions were studied on the basis of four types of small business, divided according to status - "public" or "private" - or according to geographical and cultural differences, i.e. location inside or outside Quebec.

As a result, comparisons were established between the main characteristics of the entrepreneurs and firms having opted for public financing and those that, although eligible for public financing, decided to use other methods.

In addition, significant differences were identified between the attitudes of Quebec entrepreneurs and the behaviors of their firms listed on the Montreal Stock Exchange, and those elsewhere in Canada listed, on the Toronto Stock Exchange.

Table 1.1 shows the research population divided according to the above criteria together with the chapters in which they are discussed.

1.1.2 Reasons for improving access to public financing

The action envisaged to encourage firms to use public financing can be divided into three main types.

1. Action to guide SMB owners in their decision to use public financing rather than traditional sources;

¹ Here we will be examining publicly financed firms, that is, firms listed on the stock market (also referred to as open firms or corporations), as opposed to privately financed firms. We may simplify matters by referring to "public" or "private" firms. This use of the word public should not be confused with the use sometimes made of it to describe nationalized or state-owned firms.

2. Action to create awareness among the people and institutions involved - the Montreal Stock Exchange, brokerage houses, consultants, business associations, governments of the possibilities each available, and in particular of the needs of small businessmen as identified in this research, in order to encourage and facilitate access to public financing by more SMBs;
3. Action to improve the formula or propose new measures to create interest among more entrepreneurs for public financing and investment in stock savings, while at the same time stimulating the actions of the various individuals and institutions involved.

Clearly, implementing such measures would require more specific and detailed inquiry.

TABLE 1.1
THE RESEARCH SAMPLE ACCORDING TO DISTINCTIVE CRITERIA

Sample	Criteria		
	Decision Factors	Impact of public financing	Importance of government programs
"public" firms in Quebec	Chapter 4	Chapter 5	Chapter 6
"private" firms in Quebec	Chapter 4		Chapter 6
"public" firms outside Quebec	Chapter 4	Chapter 5	Chapter 6
"private" firms outside Quebec	Chapter 4		Chapter 6

1.2 The reference model

The reference model shown in Figure 1.1 was used as a guide for data collection and classification and for analysis of the variables influencing the decision to use public financing, together with the impact of that decision on listed firms. Briefly, the model sets out

1. in the causal part, the decision of the SMB owner to seek public financing or not as being dependent, first, on the attributes of the entrepreneur himself; second, on the

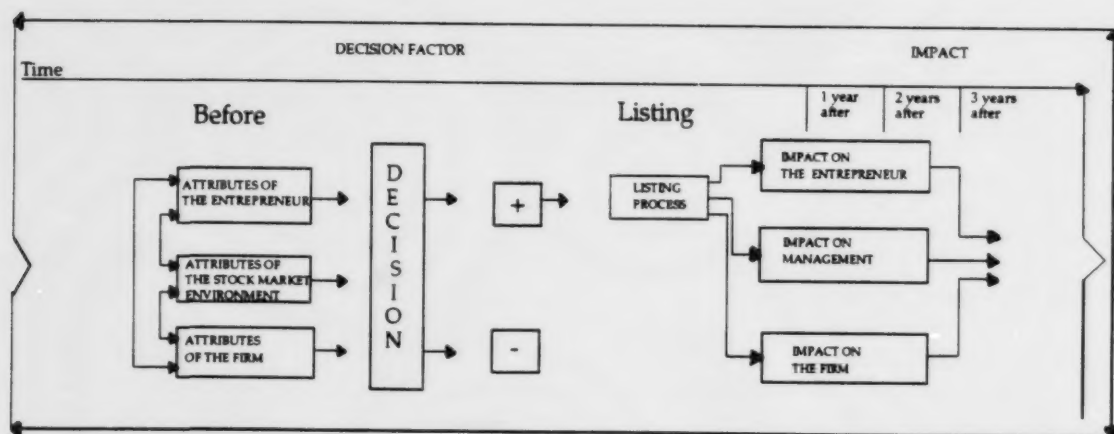
attributes of his firm; and third, on the attributes of the stock market environment as perceived by the entrepreneur;

2. in the determinative part, the decision of the SMB owner to seek public financing as affecting
 - (i) the attitudes or behavior of the owner who becomes a manager /shareholder;
 - (ii) the way the owner-manager manages;
 - (iii) how the firm operates.

In addition, the model postulates that changes may vary depending on the length of time the firm has been listed.

The same model was applied by Cooper (1989) to venture creation, and a double application, to the entrepreneur and his firm on the one hand, and the entrepreneur and financing on the other, can be found in the work of the Commission québécoise sur la capitalisation des entreprises (1984).

FIGURE 1.1
REFERENCE MODEL



1.3 Methodology

Empirical data from various sources were used to measure the importance of the variables making up the conceptual model, in particular data gathered from SMBs likely to be, or already, listed.

1.3.1 The Population

The term "SMB" (small and medium-sized business) in this research applies to Canadian firms with a net value between \$1 million and \$10 million. Qualifying firms were further divided into those located in Quebec and those located elsewhere in Canada, especially in Ontario.

The research included SMBs that had gone public, as well as those likely to do so (cf. Table 1.1).

1.3.2 The Sample

The sampling plan was established on the basis of the general problem situation surrounding public financing for SMBs in Quebec and Ontario. Table 1.2 below shows the nature and size of the samples. Two main groups of firms were identified:

1. Those that had sought public financing, that is, those that were listed either on the Montreal Stock Exchange (for firms in Quebec), or on the Toronto Stock Exchange (for those elsewhere in Canada); and
2. those that met stock market eligibility criteria and could, if they wished, be listed, but that were still considered privately financed at the time the research was carried out.

Table 1.2, detailing the units studied, shows that significant response rates were obtained for the samples established in each of the four categories. The percentage rates are high for this kind of research:

- 66% of all SMBs listed on the stock exchange in Quebec;
- almost 40% of all SMBs listed on the stock exchange in Ontario;
- 42% of privately-financed SMBs in Quebec;
- 24% of privately-financed SMBs elsewhere in Canada.

Separate questionnaires were prepared for each of the four groups and contained themes and questions of specific interest for each group. Appendix 1 provides further details about these questions.

The populations retained for the research met the following criteria:

- **Publicly-financed firms - Quebec** were SMBs that had been listed on the Montreal Stock Exchange between the beginning of 1979 and the summer of 1987, and whose stock had been traded on the floor during that period.

- **Privately-financed firms - Quebec** were growing Quebec-based SMBs in the manufacturing, trade (wholesale and retail distribution) and service sectors. They would all qualify for public financing; that is, theoretically they met the Montreal Stock Exchange eligibility criteria.
- **Publicly-financed firms - elsewhere in Canada** were SMBs from the other Canadian provinces that were listed and traded on the Toronto Stock Exchange in the summer of 1987. A total of 40% were from Ontario and the others had their head offices in the other Canadian provinces.
- **Privately-financed firms - elsewhere in Canada** were SMBs from Ontario and the other Canadian provinces in the manufacturing, trade (wholesale and retail distribution) and service sectors. They were all eligible for public financing; that is, theoretically they met the Toronto Stock Exchange's eligibility criteria.

A more precise description of the attributes of the firms studied in this research appears in Appendix 1.

TABLE 1.2
POPULATIONS AND SAMPLES

Location	Quebec		Elsewhere in Canada	
	Private (N)	Public (N)	Public (N)	Private (N)
Population	820 (1)	104 (3)	140 (4)	1800 (2)
Sample	426	104	140	500
Responses	178	69	48	116
Rate of response	41.8%	66.3%	39.2%	23.8%

- (1) Dun & Bradstreet Inc. estimate, net value between \$300 000 and \$10 000 000 in summer 1987, and estimated credit status ranging from excellent to limited.
- (2) Dun & Bradstreet Inc. estimate, net value between \$300 000 and \$10 000 000 in summer 1987, and estimated credit status ranging from excellent to good. Ontario only.
- (3) Firms located in Quebec and listed on the Montreal Stock Exchange.
- (4) Firms listed on the Toronto Stock Exchange, located in Ontario (40%) and in the other Canadian provinces (60%).

1.3.3 Analysis Methods

The results of the research were obtained from the questionnaires returned by 117 "public" firms (69 in Quebec), and 294 "private" firms (178 in Quebec). These figures represent a response rate of 66% and 43% respectively for the public and private populations in Quebec, and 39% and 24% respectively for the public and private populations elsewhere in Canada. In the opinion of the research team, these figures are sufficient to enable valid generalizations to be made for Quebec and Canadian SMBs with a net value of \$20 million or less.

The data obtained were fed into a computer and complex descriptive bi-variable and multi-variable analyses were carried out, including cross-sectioning of variables and factorial analysis.

1.4 Organization and finality of the research

As can be seen in Table 1.3, themes will be presented in the order suggested by the reference model. Individual elements will be examined first - that is, those relating to the entrepreneur himself - followed by elements relating to the firm, and finally those relating to the external environment, particularly the financial context.

Although the research concentrated on Quebec-based SMBs, the results also take account of significant differences with respect to firms based elsewhere in Canada. This allows the consistency of certain parameters in understanding the phenomenon of public financing to be identified.

Very briefly, the research presents empirical evidence of something that was previously intuitively known but not proved: that, when trying to create interest for public financing among more SMBs, the attitudes and behaviors of owner-managers must be taken into account, and not simply the financial potential of their firms.

TABLE 1.3
ORGANISATION OF THE REPORT

Category of variable	Themes studied			
Chapter 1 Table 1	Review of the literature	Decision whether or not to go public	Impact of public financing	Importance of government programs
Personal	Chapter 2	Chapter 4	Chapter 5	Chapter 6
Firm	Chapter 2	Chapter 4	Chapter 5	Chapter 6
Financial environment	Chapter 2	Chapter 4	Chapter 5	Chapter 6
	Significant differences with rest of Canada	Significant differences with rest of Canada	Significant differences with rest of Canada	

Appendix 1

HOW THE SAMPLES WERE FORMED

Publicly-financed Firms

In Quebec, there were 104 SMBs listed on the Montreal Stock Exchange at the time the research was done (summer 1987) with a net value of between \$1 million and \$10 million at the time of listing. The population was sampled as a whole, and 69 completed questionnaires were received, giving a response rate of 66.3%. This is important, since a response rate of around 30% is generally considered to be a scientifically-valid standard for this type of research.

The sample of publicly-financed SMBs from the other Canadian provinces was obtained in the fall of 1987 by sending questionnaires to some 140 firms listed on the Toronto Stock Exchange that met the same size criteria as the Quebec sample. In all, 55 SMBs from the majority of the English-speaking provinces other than Ontario responded. Forty-eight of these firms were retained for the research, the other 8 having a net value in stocks at the time of going public that was much higher than the limit defined for the purposes of the study - \$10 million. The response rate for firms elsewhere in Canada was therefore 39.2%.

Two preliminary observations seem appropriate here with respect to the samples of publicly-financed SMBs. One of the objectives of the stocks savings program is to facilitate stock market access for smaller firms. All the Quebec firms in the sample registered on the Montreal Stock Exchange had used the QSSP program. Ontario SMBs did not receive assistance from any special government program.

The second observation concerns the subsequent discovery that 28.8% of the Quebec sample had a net value in stocks slightly higher than \$10 million at the time of registration, whereas this figure rose to 37.5% of Toronto-listed sampled firms. For research purposes, therefore, the maximum limit had to be raised to \$15 million in Quebec and \$20 million in Ontario. The decision to retain these firms was based on the fact that the \$10 million criterion is purely arbitrary in determining the size of a small or medium-sized business,

and may well be too low for SMBs able to consider stock market financing, as was recently suggested by the Montreal Stock Exchange President (Riverin, 1989)². Second, it was felt that as many responses as possible should be used, given the wealth of information contained in the 18-page questionnaire.

A third reason lies in the fact that the qualitative and sociological nature of the analysis reduces possible disparities between respondents despite the difference in the size of the firms. Therefore, in the context of this research, the two populations of publicly-financed firms were comparable.

Privately-financed Firms

A list of private firms potentially eligible for stock market registration was provided by Dun & Bradstreet Inc.

In Quebec, 376 questionnaires were sent to firms with an estimated net value of between \$300 000 and \$10 million whose credit rating varied from excellent to average. In all, 153 responses were received and compiled, giving a response rate of 43.9%.

It was considered useful to verify the results by using firms that were not on the Dun & Bradstreet list, but were identified by underwriters as having the potential to go public. Fifty additional questionnaires were sent out, 25 of which were returned.

A total of 178 out of a sample of 426 privately-financed Quebec-based firms returned the questionnaire, and the data were fed into a computer for analysis. This represents a response rate of 41.8%.

In Ontario, 500 questionnaires were sent out to firms with an estimated net value between \$300 000 and \$10 million and a credit rating of excellent or good. In all, 116 completed questionnaires were compiled, a response rate of 23.8%.

To sum up, the high response rates are a reflection of the efforts made by the researchers the importance of the issue as perceived by the respondents. The main objective of the data collection was to obtain the highest response rate possible from firms in Quebec, where the most significant changes in attitudes and behavior of SMB heads with respect to public financing have been observed since the introduction of the QSSP in 1979.

² Mr. Bruno Riverin, President of the Montreal Stock Exchange in a press conference, expressed the hope that the minimal level for a stock issue would be raised to \$15, and even \$20 million (see *La Presse*, March 22, 1989, p. C - 9)

A satisfactory response rate of 39.2% was obtained for publicly-financed firms elsewhere in Canada, and an acceptable rate of 23.8% for privately-financed firms. This meant that comparisons could be made between trends and attitudes among Quebec's entrepreneurs and entrepreneurs elsewhere in Canada with respect to seeking public financing for expansion purposes.

The data collection instruments included four questionnaires previously validated among business people and people from the stock market community. The questionnaires (a copy can be obtained upon request from the researchers) contain common divisions or divisions specific to the firms being questioned. The themes covered for private firms were:

1. Factors supporting the decision to seek public financing;
2. Attributes of the entrepreneur and the firm;
3. Impact of the various programs on the decision to seek public financing.

For listed firms, the same headings were used so that comparable data were obtained for all sample groups, and a fourth heading was added:

4. Impact of public financing.

Questions relating to the financial environment were adapted according to geographical location - Quebec on the one hand, the rest of Canada on the other - and this affected Ontario firms in particular:

5. Financial environment - Quebec or the rest of Canada.

Chapter 2

FACTORS RELATED TO THE DECISION TO USE PUBLIC FINANCING: LITERATURE SURVEY

2.0 Introduction

A good deal of research has been done on the ability of various countries to provide easier access for entrepreneurs to risk capital (Springate, 1972; Legoff and Rosenfeld, 1980; Economic Council of Canada, 1982; Kierans, 1985). This interest results from the growing recognition of the contribution of small and medium-sized business to the economy and employment (Royal Commission on economic union and development prospects in Canada, 1985, Vol. 2; Vallerand, 1985; Desroches, 1986). Particular attention has been paid to the financial structure of SMBs (Saint-Pierre, 1981; Groupement québécois d'entreprises, 1984; Gasse *et al.*, 1984) subsequent steps taken by governments to improve access for SMBs to equity capital and to reduce debt/equity ratios. The effect of these steps has been to improve SMB stability in an highly volatile interest rate environment. At the same time, other research looked at why firms may wish to obtain stock market listing, and tried to identify the reasons or factors affecting the decision. Two constant elements can be seen in this literature.

First, it seems that the decision to obtain financing by issuing shares is linked to a set of complex factors related to the entrepreneur himself, the firm and the financial environment.

It also appears that, since access by SMBs to public financing is relatively new in Canada (Gasse *et al.*, 1984: 68), and fairly recent in the United States (Commission québécoise, 1984: 57), very little research is available on the phenomenon, and the behaviour of owner-managers of listed firms has rarely been analyzed.

For these reasons, this study pays particular attention to the changes in the capital structure of the SMBs studied, and attempts to identify factors affecting the decision to "go public". However, at the outset it is useful to list the factors already identified in existing literature, to assess their relative importance, and to determine their empirical validity.

It should be noted that this examination of previous research formed the basis for the reference model previously presented in Table 1.1 relating to:

- the individual attributes of the entrepreneurs;
- the attributes of the enterprise;
- the financial environment.

This threefold investigation provided the guiding structure of this research. Inadequacies in previous studies, together with the questions requiring deeper examination, are identified in the following sections.

2.1 The personal attributes of the entrepreneurs

J.-M. Toulouse has been at the forefront of research in Quebec on the subject of entrepreneurs, small business and financing for more than twenty years. In a report for the Commission québécoise sur la capitalisation, Toulouse (1984) suggests that the question of financing or capitalisation of firms is not, in fact, a problem of financing or capitalisation, "... but rather a problem of strategy, in that a number of entrepreneurs who have achieved a certain level of growth decide to protect what they have rather than commit themselves to further growth" (p.15). Later, he adds that "... a good deal of research leads to the conclusion that obstacles to capitalisation are composed as much of behaviour as of objective capital availability" (p.22). In conclusion, he suggests that the members of the Commission "... concentrate on the entrepreneur and his behaviour [...], since it is the most important aspect in terms of change, as well as being the most important factor in the capitalisation decision" (1984: 26-27).

Among the many existing financing models for dynamic SMBs¹, the Commission québécoise opts unreservedly for capital financing, which, it says, "... should be a normal business path, particularly for rapidly-growing firms" (1984: 30).

¹ Especially firms in the manufacturing sector and those in the productive tertiary sector, according to the Commission québécoise's mandate (1984: 4).

The above observations led us to examine the personal factors, or attributes, of entrepreneurs that could affect their choice of how to finance their firm's growth.

To date, sociological, psychological and management research literature has not dealt in any depth with the relation between the attitudes or personality of the entrepreneur himself and his decision to use external equity financing.

Yvon Gasse, like J.-M. Toulouse, a pioneer in entrepreneurship research in Quebec, has drawn up a basic typology. In an article published in 1985, he reviewed the various factors and intervention models to foster entrepreneurship development. In his conclusion to the part dealing with the attributes of the entrepreneur, Gasse groups the various themes studied by authors and researchers in the field under six headings (Gasse, 1985, p.10):

1. The need for achievement and success;
2. Creativity and initiative;
3. Risk-taking and identification of objectives;
4. Self-confidence and audacity;
5. The need for independence and autonomy;
6. Motivation, energy and commitment.

We believe that the decision to use public financing to fund business growth depends particularly on two attributes of the entrepreneur himself: his need for independence and autonomy, and his need for achievement.

2.1.1 The need for independence and autonomy, and the need for achievement

By definition, an entrepreneur is someone who builds a world he controls: his firm, which he maintains as an image of himself (Toulouse, 1984: 7). He is also energetic, confident, sure of himself, independent and completely devoted to realizing his objective, the success of his firm (Gasse, 1980, 1981, 1985; d'Amboise, 1989: chapter 3); but in his own way (de Vries, 1977) and at his own speed (Grieve, 1972; Facsym, 1982).

When the firm reaches the growth stage, a typical entrepreneur generally hesitates to bring in external capital, since he sees it as a threat to his personal and organizational autonomy, and as a loss of power and control over the objectives he has set and the methods available to him for achieving them (Litvak and Maule, 1971; Gasse, 1978; Saint-Pierre, 1981; Gasse, 1984).

However, the decision to use external financing and the choice of the financial instrument (debt or equity) to be used also depends on the entrepreneur's need for achievement (McLelland, 1969; Brockhaus, 1981, 1982, 1986), or his need for self-

accomplishment (Maslow, 1954; Gasse, 1979, 1986). The two research projects discussed in the following pages establish an entrepreneurial typology based on the growth orientation given to the firm as a result of the entrepreneur's need to retain control over it.

Laufer (1974) speaks of *owner-managers*, *innovators* and *artisans*. He observes that owner-managers and innovators accept and encourage the growth of their firm, and are concerned mainly with self-accomplishment. In general, they have a higher level of education. The artisans, on the other hand, do not want their firm to grow, and are extremely concerned with maintaining their personal autonomy. Owner-managers, especially those who launched their business because they were dissatisfied with their previous employment, seem to be directed towards holding and maintaining power within the firm. Some of them will permit limited growth provided it does not threaten the organization's financial independence; others, however, tend to reject any kind of growth in order to keep full control. This typology, and the research on which it is based, also shows that the level of education and the previous professional experience of owner-managers may affect their willingness to use external equity financing.

Knight's (1983) classification of various entrepreneurial styles leads to the same conclusions. He establishes three profiles:

1. The *promoter*, described as an owner-manager trained in marketing or sales and having experience of finance and production or sales;
2. The *artisan*, described as an owner-manager skilled in technical or operational fields;
3. The *general manager*, described as someone who manages his firm as though it were at the start-up stage, being closely involved in production, marketing and finance.

According to Knight, the promoter has no problem seeking outside financing (public financing, bank loans or any other type), the general manager is less inclined to do so, and the artisan is totally opposed to it.

These observations tend to suggest that the personal attributes of the entrepreneur are relatively important in explaining his decision to "go public". However, the importance of these empirical attributes and their validation, especially for firms having opted for public financing, have not been considered in previous research.

2.1.2 Socio-psychological variables

If, as we have just seen, public financing for SMBs is fairly new in Canada, and if its use by fast-growing firms depends largely on the attitudes and behaviour of the entrepreneurs themselves, it is worth checking to see if other socio-psychological factors can also be used to distinguish entrepreneurs' choice of external equity financing. Factors such as age (Brockhaus, 1982: 53; 1984: 29), level of education (Gasse, 1985: 64-65), whether or not additional courses in management have been taken (Gasse, 1984: 67-68), the number of years at the head of the firm, and other similar variables, have already been suggested as explaining entrepreneurial potential to a certain extent, and as being significant with respect to entrepreneurial development in various contexts.

The contribution of this research, among other things, is to verify the predictive value of these variables as they affect the "going public" decisions of eligible Canadian SMBs.²

2.2 Attributes of the firm

Although the choice of the method of capitalizing a growing SMB "... depends first and foremost on the attitude of the entrepreneur" to the choices open to him, the Commission québécoise sur la capitalisation des entreprises (1984: 27-33, 63-64) points out that public financing implies certain strategic and structural conditions for the firms concerned.

"Going public" means sharing the decisional power and ownership of the firm to some extent. The entrepreneur's attitude to this will vary "... according to the firm's stage of development, the type of activity in which it is engaged, and its objectives" (Commission québécoise, 1984: 35). More precisely, the Commission specifies that the first public issue usually corresponds to the third stage in the firm's life cycle, after start-up and the first time outside owners and funds are brought in (1984: 109). J.-M. Toulouse (1984: 17) adds that this stage corresponds "... to mature firms [...] where ownership is already shared [...] and where the entrepreneur chooses growth for his firm".

At this point, the firm is already engaged in continuous, realistic strategic planning, generally has a structured communications system and a system to control achievement of its objectives, and often it uses outside advisors or has a board of directors. As Patricia Johnston points out, in other words SMBs considering public financing tend "... to demonstrate good management and depth" (The Toronto Stock Exchange, 1980: 35-37).

² The term "capitalisation" here is taken to have the same meaning as in the report of the Commission québécoise (Commission québécoise, 1984): increase in capital.

This "professional management" stage, as Steinmetz (1974) calls it, is inevitably accompanied by some kind of financial structuring, since stock market eligibility and the sale of shares to an individual or institutional investor, on a secondary market, requires a clean bill of financial health and clear planning of the firm's objectives, together with the means to achieve them.

To sum up, the age of the firm, the importance accorded to management and strategy by the owner-manager, the extent to which his business plan is established and the existence of a financing plan are some of the elements characterizing firms with stock market potential. The predictive value of these elements will be verified later in this research.

2.3 The attributes of the financial environment

The financial environment also has a determining effect on the entrepreneur's decision to use outside financing. Three environmental aspects are known to be of particular importance in the decisional process: taxation, the activities of lending institutions and the nature of the securities market.

2.3.1 Taxation

Taxation affects the choice of external capital sources in two basic ways.

First, on a more generic level, as interest on the debt is tax-deductible, bank loan or debt financing is often the least expensive way of financing a firm. During inflationary periods, the real after-tax cost may even be negative, which clearly favours the debt option. Favourable taxation conditions and lower tax rates are also available to private Canadian corporations.

These generous provisions and lower rates are generally no longer available once the firm has moved into public financing. Although there is no easy way of identifying the influence of tax laws on the decision to use public financing, it can nevertheless be said that both federal and provincial tax rules tend to favour debt financing and private control rather than stock financing.

2.3.2 Lending institutions

It has been said that the nature of the Canadian capital market has also encouraged SMBs to use bank loans. In addition, many federal and provincial programs have been designed to provide loans for SMBs which find it difficult to obtain funds. A good deal

of research (Thornton, 1981; Wynant *et al.*, 1982; Gasse, 1984; Dun & Bradstreet, 1986) confirms that SMBs usually opt for loan financing, and that on the whole they are satisfied with the process. Dun & Bradstreet's (1986: 10) research explains that medium-sized firms rarely opt for public financing because they simply do not need funds. It can therefore be said, at least for Canada, that sufficient capital may be available for a majority of firms in the institutional financial environment, which once again tends to favour loan financing and private control.

2.3.3 *The securities market*

The securities market also affects the environment for the firm's decision to "go public". Clearly, there is no precise way of deciding whether or not a particular firm has a favourable environment for an initial public offering. One approach sometimes used in research is to compare the number of initial public offerings in two different countries for the same period. Research by the Economic Council of Canada (1982) indicates that there were 234 times as many small initial public offerings (i.e. less than \$2 million) by manufacturing firms in the United States as in Canada between 1977 and 1981. This ratio is extremely high compared with the ratio of the total number of firms (7:1) or the Gross national Product (9:1) between the two countries.

Five hypotheses have been suggested to explain this difference:

- In Canada, the internal regulations of some financial institutions (life insurance companies, trust companies and pension funds) may prevent them from participating actively in the initial public offerings market. Their lack of enthusiasm could put small firms off the stock market, since the cost of equity can be high.
- In the United States, the most active promoters on the IPO market are regional underwriters. Between 1977 and 1981, they managed 79% of all initial offerings and 92% of those below \$10 million. In Canada, the brokerage industry is dominated by national underwriters who may be less interested in smaller offerings, for the obvious reason of economies of scale. However, although there are fewer regional underwriters in Canada, this factor may not be very significant in explaining the relative difference of 40% in the number of new initial offerings between the two countries. In Quebec, the QSSP has had a considerable effect on the public financing infrastructure as a whole, whether at the level of brokerage firms, corporate financiers or technical and academic research in the field (Secor, 1986: 61-64).

- The third reason often put forward to explain the difference is that the average Canadian investor is less willing to take risks than the average American investor. However, in Canada, initial public offerings in risky economic sectors related to natural resources continue to increase.³
- Fourth, admission criteria for the Toronto Stock Exchange, the main one in Canada, may appear too strict to many firms that might otherwise have considered an initial public offering. While this may have been the case in the past, most securities stock exchanges have now rationalized their procedures with respect to IPOs.⁴
- Fifth, the costs of stock market admission and registration may be higher in Canada, which would tend to dissuade firms from using public financing.⁵

In this fifth category, two costs are generally associated with an initial public offering: the offering cost, i.e. subscription fees, lawyers' and auditors' fees, printing expenses, etc. - costs that are proportionally higher for smaller offerings in both countries - and an *underpricing* cost, i.e. the difference between the offering price and the listed share value after issue.⁶ If this underpricing is systematically higher in Canada than compared to the U.S., then it would encourage firms to use debt rather than seek external equity capital.⁷

In addition to these negative factors affecting the "going public" decisions, relatively little information is available on the process followed by owners in going public. More specifically, little information, if any, is available on how entrepreneurs go about identifying brokerage houses and their reasons for choosing a particular underwriter.

³ However, in Canada, an accredited stock plan exists.

⁴ Among others, steps taken by the Toronto Stock Exchange and the Ontario Securities Commission (OSC), such as Formula 20, the Exchange Offering Prospectus (EOP), the automatic transaction system for over-the-counter shares, and the efforts made by the Montreal Stock Exchange and the Vancouver Stock Exchange to improve the chances of small firms to use equity financing (See Briggs, 1983).

⁵ In addition, Canadian deregulation in the brokerage field is 10 years behind the United States.

⁶ For example, a firm that is 10% underpriced by the brokers could see its shares rise by 10% at the end of the first day on the market. The difference between the quoted value of the shares and the amount paid to the firm by the broker is the "underpricing" of which the firm is a victim.

⁷ Some interesting results relating to underpricing are presented in Appendix 2.

Their sources of information and the difficulty of either choosing an underwriter or having their prospectus accepted must also be examined. Their level of satisfaction or dissatisfaction with the contacts established with the securities market, and the efforts generally made to negotiate public financing, need to be assessed. In addition, it would be useful to understand how each owner can compensate for the disadvantages of his own particular enterprise situation, or simply how he can improve his chances of obtaining the financing he wants, by carefully preparing the required documentation and information to ensure a properly valued initial public offering.

2.4 Conclusion

Based on this literature review in the area of external financing for small and medium-sized businesses, it is clear that only a limited and often contradictory research is available. In particular, this review has revealed that the literature on the personal attributes of entrepreneurs, the attributes of the firms and those of the financial aspect of public offerings is fairly fragmented, and interrelations between the various hypotheses have not been established. No link or empirical validation has been made between the diversity of the strategies and decisions relating to external equity financing on the one hand, and the particular aspects of the management style or the firm itself - which could in turn affect the strategies and decisions relating to financing - on the other.

Although the research on the personal attributes of owner-managers also reveals just how much the financing orientation depends on the social and psychological characteristics of the entrepreneur, and on the managerial aspects of the firm, no empirical evidence is available to verify these conjectures.

More precise information is needed on how the psychological attributes of the entrepreneur can influence his management style and how they can be linked to variables such as the level of education - which itself may affect the management style and, consequently, the likelihood of opting for public financing. It may also be interesting to establish the extent to which factors such as previous professional experience, the type of firm, the importance of self-accomplishment or the need for autonomy can influence the level of commitment to pursuing growth objectives or the desire to innovate.

It seems important, in analyzing the attributes of the firm, to study a number of factors such as size, stage of development, level of diversification, and so on, in terms of their impact on the decision to use public financing.

It would then be interesting to consider the consequences of "going public" on the various enterprise functions, such as production, marketing or financial control. In

particular, it may be useful to assess how a firm having obtained external equity impacts the entrepreneur's need to control. The number of years the firm has been in existence and the experience of the owner-manager are also useful factors for explaining the fact that some firms actually find it easy to expand - it has been suggested that enterprise development and growth necessarily imply problems of adaptation and adjustment for the entrepreneur, both in financial and managerial terms.

Other variables such as size, stage of development, the nature of the firm's activities and the existence or lack of a growth policy have also been quoted but rarely validated empirically.

Finally, environmental factors said to explain the infrequent use of equity financing by small and medium-sized firms can be summarized under five headings: legal restrictions and internal investment policies of institutional investors, the small number of regional underwriters, a mitigated attitude to risk by entrepreneurs, stock market eligibility conditions and share issue costs.

The obstacles facing SMBs in raising equity capital can be classified into two groups. The first group includes factors related to the disadvantageous situation of small firms on the securities market, due to their nature or their size, or the attitudes of business communities (especially financial institutions and institutional investors), and also due to the psychology of the entrepreneur himself and the growth orientation he favours. The second group includes some unfavourable tax provisions or banking conditions that may favour either debt financing or maintaining of the private status.

What is intended here is not so much an explanation of why SMBs use or do not use the external equity markets, but the establishment of a base from which to understand why and how some entrepreneurs seek equity capital by "going public". The following research and empirical validation of determining factors from the three predictive categories identified in the reference model should bring about a better understanding of the mechanisms underlying the decision to "go public".

The next chapter contains a historical view of the measures adopted by governments to encourage SMBs to use public financing. It complements the literature survey in this chapter, and serves as a prerequisite to understanding the research framework. It also provides the necessary context for judging the importance of this study and understanding the results of the study. It is hoped that the study as a whole will lead to a better understanding of the interest - or lack of it - shown by SMBs for "going public".

Appendix 2

IMPACT OF UNDERPRICING ON THE "GOING PUBLIC" DECISION

Till the early 1980s, very little systematic Canadian research on the extent of underpricing of initial public offerings in Canada was available. A large part of the research on the subject was based on empirical work carried out at the end of the 1960s over a relatively short period. Shaw's (1971) results indicate that investors who bought shares in initial public offerings during the periods 1926 - 1928 and 1956 - 1963 obtained negative yields on their investments in comparison with stock market listings as a whole. Three other studies (Kryzanowski et Philan, 1977; McQuillen, 1971; Héroux, 1979, 1985), assessing yields of initial public offerings, carried out towards the end of the 1960s, conclude that, on average, underpricing is situated between 30% and the valuation of the IPOs. Once again, this information presupposes that the costs of subscription and underpricing are not the only important factors in the decision of entrepreneurs avoid "going public".

Based on this limited research, a report by the Economic Council of Canada in 1982 stated that "on the whole, the owners of small and medium-sized firms have sacrificed around 47% of the value of their shares to get access to the public market". This may explain why SMBs issue so few shares. The study recommended a limited form of government intervention to counter this exaggerated underpricing and encourage entrepreneurs to use equity financing.

However, recent research by Jog (1987) provides some new and contradictory results. His results show the average degree of underpricing to be nearer to 10%, which is slightly lower than the figures reported in comparable American research. It can also be observed that the extent of underpricing varies considerably from one firm to another, and that around 40% of initial offerings in the sample taken were in fact underpriced.

Research on the criteria used by investors to assess the valuation of the initial public offering also failed to reveal the direct effect of the size of the firm on share valuation. According to a study of the major individual investors of twelve Canadian brokerage houses, the most important factors in fixing the initial share price were "possibilities for future profits" and "the quality of management". The possibilities for future profits by the firm and its position with respect to its industrial sector were also considered very important (Kantor, 1984-1985). A previous study revealed that total assets before the share issue, the level of liquidity and the firm's history were also considered when estimating the list price of initial offerings (Kantor, 1983). The main implication of these results is that the most frequently-used criterion - "possibility for future profits" - is based on a highly subjective assessment. It can also be presumed that the firms could themselves increase the listing price of their shares by presenting data supporting a clear vision of the firm's financial stability and its possibilities for future growth. Investors also suggested that more than a third of the variables affecting the initial price could be directly influenced by the owners themselves in the short term, by making certain adjustments before the offering, and that up to 80% of the variables could be influenced in the long term by the addition of other appropriate measures (Kantor, 1984-1985).

What conclusions can be drawn from these results? The degree of underpricing may well have decreased over time, but the phenomenon itself may also be more usual on the Canadian stock market than on the American one. Small and medium-sized firms are also probably disadvantaged to a certain extent when using public financing, given the lack of certain skills and experience and their less well-established relationships with brokerage houses.

Clearly, however, the financial health of the firm, its economic possibilities, the quality of its management and how seriously its expansion plans are defined and pursued, are all vital factors in investor's decisions with respect to the purchase of an initial public offering.

Chapter 3

FINANCING GROWING SMBs: A HISTORICAL OVERVIEW

3.0 Introduction

A number of more or less fortunate initiatives on the part of governments, stock exchanges and financial institutions have appeared with the intention of offering new forms of financing to SMBs.

The *Second Market* introduced in France, for example, has been an undeniable success even in the difficult economic climate of the day. In North America, many efforts have been made to make access to public financing easier for SMBs and to increase the interest of savers and investors in these economic sectors.

This chapter sets out a brief history of the development of public financing for SMBs in Canada. The case of Quebec is presented first, followed by Ontario and the other provinces. The development of legal measures and taxation, and their effects on the orientations of institutions and others will also be examined.

3.1 The Quebec model

Historically, the Government of Quebec has shown a great deal of interest in the financing of SMBs, mainly "to try to face up to the problems inherent in the structure of Quebec's economy" (Sales, 1983: 3).

Roger Worth, who manages the Public Affairs Service at the Canadian Federation of Independent Businesses, goes even further when he says that, "in contrast to the other provinces, the Quebec government has always recognized the economic importance of small business and has acted to protect and encourage it" (1980: 11).

In this field, the question asked over and over again is not whether the state should intervene, but rather how it should do so (Sales, 1983: 41; Parizeau, 1985: 6; Royal Commission on economic union and development prospects in Canada, 1985b: 3; Kierans, 1985b: 19).

Over the last fifteen years, a large number of academic and business publications have reported studies and research with recommendations on how to help SMBs, the "new Golden Fleece" (Vallerand, 1985: 1) that has replaced big business to become the "driving force of economic growth in our society" (Bourassa, 1984: 10). Since 1982, the rate of small business start-ups has been very high.

Two fundamental questions arise from these publications:

1. Should governments intervene directly, by facilitating small business start-ups, or indirectly, by creating a favourable climate for start-ups?
2. If they decide to intervene, should they do so through the traditional - even if contested - method of grants, or should they use other methods, such as tax benefits?

Large firms generally reject the idea of direct government intervention in the economy, under the pretext that political considerations (regional economic development, for example, or stimulation of particular sectors to the detriment of others) will interfere with decisions that are essentially economic in nature (Desroches, 1986a: 11-12; 15-18). But the Chambers of Commerce never miss an opportunity to express their disapproval of government intervention through grants, thought to subsidize ease and mediocrity (Desroches, 1986a: 18-20).

Small and medium-sized firms (SMBs), the major beneficiaries of grants, are more cautious in their reaction (Desroches, 1986b)¹. In general, they disapprove of grants that give an unfair advantage to one enterprise over its competitors, or grants that create artificial competition by keeping lame ducks in the race; but they approve of grants to promote fast growth, exporting or research and development - given that SMBs, unlike big businesses, do not have sufficient financial means to achieve these objectives alone. Theory would have it that SMBs, being more fragmented and diversified, multiple and flexible, often need "... government initiatives to compensate for the major disadvantages of being young in age and small in size" (Bulloch et al., 1985: 3) if they are to realize their potential.

And governments, torn between their economic and political objectives and the dynamism of small business, not to mention the general and ever-increasing public enthusiasm for this economic sector, try to do what they can, as effectively as possible, taking account of the

¹ In this research, the author carries out an in-depth analysis of the attitude of small business owner-managers to the cultural (pp. 12-24), organizational (pp. 25-40) and individual (pp. 41-47) aspects of enterprise grant programs.

usual financial constraints. And Quebec, not having the same powerful industrial structure that Ontario has (Sales, 1983), based on the steel and automobile industries, has had to innovate earlier in terms of help for small firms.

3.1.1. The period between the 1960s and the 1981-82 recession²

In the mid-1960s, despite other major investments in educational and social institutions, the Quebec government had already created the Société générale de financement (SGF). The SGF's first mandate was to rescue firms - often family firms - and set them back on the road to growth. Volcano, Forano, John Meunier, Tricots Lasalle and many others, such as Artopex, all benefited from this kind of state aid. In the early 1980s, during the economic crisis, the SGF played a more important role in the province's economy by tackling the major sectors of the Quebec economy: pulp and paper, shipbuilding, high energy users such as the aluminium or magnesium industries (where the province has an unquestioned comparative advantage), petrochemicals, etc. In doing so, it left the small business community and moved on to the world of big business.

This change of direction was made easier by the fact that, in 1971, the province had instituted another organization to help small business development: the Société de développement industriel (SDI), whose original mandate was to provide grants and administrative support for small firms. There again, however, soon money was being given to just about anything that moved in the teeming world of small business. Finally, in 1985, the new government, faced with even more limited financial resources, realized that it was completely useless to subsidize, among other things, all the door and window manufacturers in the Bois-Francs area. It was far better to save what financial resources were available for the internationally-dynamic sectors and firms. The result was that, in 1985, the SDI's programs were reoriented.

In the mid-1970s, faced with an increasingly competitive world economy and its own limited budget, the government was already thinking of using public investments to help SMBs. The SGF had already gone down this road, with mitigated success, and had subsequently to be privatized.

In 1978, the Government of Quebec launched the SODEQ concept: Sociétés de développement de l'entreprise québécoise. These bodies were responsible for gathering public funds using the carrot of major tax benefits, and investing them in dynamic small or medium-sized firms. However, the SODEQ experience was short-lived, strangled by legislative

² Readers wishing to have more specific information on the nature of the programs, their implementation and an assessment of their results is invited to contact the government bodies responsible for the programs. This section is intended simply to identify points of comparison between government programs and equity financing.

constraints: the obligation to reserve 70% of their funds for risk capital, their incredibly large numbers and some instances of embezzlement tarnished their reputation and prevented them from reaching the stage at which they would have become effective. The Caisses d'entraide économique also experienced some setbacks.

In 1979, the government finally introduced the Quebec Stock Savings Program (QSSP), both to lighten the fiscal load of top wage-earners and to help the more dynamic SMBs obtain public financing, as large firms did; and also with the aim of stimulating the Montreal Stock Exchange and introducing the province's taxpayers to the stock market.

In fact, the program consisted of transferring the perceived fiscal benefits of the SODEQs directly to small firms. The QSSP scheme was left on the shelf for nearly two years, until the economic recovery in the fall of 1982 and spring of 1983. In 1983, Finance Minister Jacques Parizeau introduced a bill allowing financial institutions to administer QSSPs for their customers. Until then, the province's taxpayers had used QSSPs mainly to invest in big firms such as Alcan, Bell Canada and the National Bank.

3.1.2. The economic crisis of 1981-82 and subsequent years³

The 1981-82 economic crisis highlighted just how vulnerable Quebec's SMBs were, with their generally limited initial capital and their inability to have a stable capital structure simply on the basis of reinvested earnings.

At the same time, the provincial government was faced with its own extremely limited financial resources - to the extent that, during the crisis, subsidies had to be reduced and state guarantees were needed to prevent the worst from happening: the Biron plans, I and II, were no more than guarantees for credit margins; in other words, temporary life jackets to help SMBs survive the storm.

After the crisis, the government, led by Trade and Industry Minister the Hon. Rodrigue Biron, created the Commission québécoise sur la capitalisation des entreprises (the Saucier Commission) to find longer-term solutions to entrepreneurs' capitalization problems.

Among its recommendations, the Commission suggested the implementation of the QSSP Investment Fund, a formula based on the SODEQs, but with fewer restrictions. When the government did nothing to act on this recommendation, it was taken up by the private financial institutions.

The Commission also recommended setting up the QBICs, Quebec Business Investment Companies, intended to help small firms that were too small for QSSPs but that nevertheless

³ See Note 2.

wanted to offer their people (executives, employees and friends) similar fiscal advantages. However, the QBICs do not have all the advantages of the QSSPs, particularly in terms of visibility and public recognition.

To sum up, government assistance to small business became more sophisticated over the twenty-year period between the mid-1960s and the mid-1980s. The private sector itself is now used to the maximum, both through financial institutions and public investment. The QSSP scheme still provides an example for other governments, and at the same time enables Quebec's small firms to obtain better capitalization.

Other organizations and bodies have also appeared on Quebec's financial market during the last few years: The Société d'investissement Desjardins (SID), for risk capital and long-term financing, and its subsidiary Crédit industriel Desjardins (CID)⁴, for commercial loans and short or medium-term financing, the FTQ's Fonds de solidarité and other risk capital corporations such as Innocan, Novacap and so on, which include participation by financial institutions such as the Caisse de dépôt et de placements, la Laurentienne, the National bank, the SGF and many big pension funds. The increasingly important role played by foreign banks and the credit unions, especially since legislative changes in 1983, is also worth noting.

In short, there are now all kinds of financing alternatives on the market, and today's managers of SMBs have a great variety of choices available to them of financial partners and alternatives.

3.2 The Ontarian model and the other provinces

As in Quebec, the other provincial governments have also come to realize the importance of enabling SMBs to access the stock market. In fact, even before the 1981-82 recession, Ontario was the first province to recognize explicitly the economic contribution of SMBs. In January 1978, the Ontario government created a pilot program which, the following year, went on to become the Venture Investment Corporation program. Since September 1985, all the other provinces have copied this idea, giving tax deductions and direct assistance through cash grants to investors and entrepreneurs who qualify for the Small Business Expansion Corporation programs.

Although these programs vary in their approaches to providing financial help to SMBs and investing corporations, in general they follow two models intended to facilitate small business access to stock financing.

The first model is based largely on the famous Ontario program, the Small Business Development Corporations (SBDC). This program offers tax credits to firms or grants to individuals.

⁴ Readers should note that recent (1988) changes have been made to the Desjardins organization chart.

The SBDC program was created in July 1979 to replace the Venture Investment Corporations, and, during its first four years of existence, generated investments totalling \$165 million in some 400 Ontario small firms. At the end of June 1986, the figure was \$331.4 million, and in January 1988, \$388 million. It is interesting to note that a large part of these investments went into manufacturing sector firms, mostly in the Toronto area and central Ontario.

At the beginning of the 1980s, the average investment was in the region of \$150 000, and recently has risen to \$200 000. Quebec (with its SODEQs), Saskatchewan, Alberta, Prince Edward Island and British Colombia have also established similar programs.

The second Ontario model - the one adopted by Manitoba, New Brunswick, Newfoundland and Prince Edward Island - offered public funds to eligible firms. In most cases, these government contributions took the form of loans, with or without collateral, at low or zero interest rates, over periods between seven to twelve years.

The main aim of all these investments was to channel external financing to firms needing it. The fundamental difference between these programs and QSSP was the creation of an intermediary corporation which, in turn, invested in the firms. According to Gadbois (1987), small firms have benefited from some \$656.6 million in investments through these programs. In fact, it is more realistic to suggest that about half this figure can be attributed to government programs. The average value of the investments ranged from \$50 000 to \$250 000.

Despite their success, the practical application of these programs was not straightforward. First, the \$656.6 million in investments generated over the last six years was still far below what is needed. Second, they help only SMBs wanting less than a quarter of a million dollars and employing less than 200 people. Third, statistics on investment yields are not always available - but are necessary if the value of the programs is to be judged. Fourth, contrary to the QSSP, these investments are essentially non-negotiable and non-transferable. Therefore, the shares cannot be exchanged, which means that the investor cannot check the market value of the investments on a regular basis. In fact, it was mainly because of this last factor that Alberta decided to create the "Alberta Stock Savings Plan", based largely on QSSP model.

3.3 Stock market initiatives

The contribution of Canada's stock exchanges to making outside capital available for SMBs' expansion needs is also considerable. The primary role of the stock market is to obtain investment funds for entrepreneurs in the form of common shares by listing the firm's shares on the stock exchange. As well as providing investment opportunities for investors, stock exchange listing also enables funds to be transferred and the market value of investments to be assessed continually. These two points mean that stock exchange listing criteria are extremely important, as are the provincial Securities Commission regulations.

They bestow an importance to the stock exchange initiatives that can be compared to government action.

3.3.1 The case of Ontario and the Toronto Stock Exchange

The case of the Toronto Stock Exchange and the Ontario Securities Commission illustrates the importance of stock exchange initiatives.

The 1966 provincial law gave the Ontario Securities Commission the power to govern all stock market transactions in Ontario. Since then, the Ontario Securities Commission has enacted a number of rules covering disclosure of information on stock exchange listed firms to protect investors. However, as the costs related to preparing and disseminating information on public companies are fixed, the burden is felt more acutely by small firms. In addition, the Toronto Stock Exchange charges extra registration fees.

These costs have always been a major obstacle for SMBs seeking listing. In 1983, in an attempt to reduce them, the Toronto Stock Exchange established a simplified form called the Exchange Offering Prospectus (EOP), in the form of straightforward questions and answers. It was intended to cut down the legal costs so that SMBs, usually in the manufacturing sector, can benefit from public funds through the stock market. This initiative has achieved considerable results.

Although the EOP formula reduces the cost of stock market access, the other financial obligations associated with registration nevertheless tend to limit the number of small firms wanting to list on the Toronto Stock Exchange. To promote over the counter stocks (OTC), the Ontario Securities Commission and the Toronto Stock Exchange introduced jointly an automatic transaction system called COATS, in March 1986.

The main objectives of this initiative are to provide a market for the stock of firms too small to register on the Toronto Stock Exchange, but that are nevertheless looking for equity and capital funding. The program uses a highly effective information and operational system. In January 1987, 1,102 securities were already traded through COATS, and this figure had risen to 1,250 by January 1988. COATS trading activities for the year 1987 were estimated at 443.7 million shares, for a total value of \$1.86 billion.

3.3.2. The case of Quebec and the Quebec Stock Savings Program

The Quebec stock savings program, introduced in 1979, had three precise objectives:

1. To reduce the tax burden of high-income taxpayers;
2. To foster better capitalization of Quebec's firms;
3. To increase shareholding by Quebecers.

Everyone involved at the time agreed that there was a need to correct the high marginal tax rates experienced by taxpayers, to address the equity problem of SMBs (under-capitalization), and to encourage new investment habits of Quebecers (increased shareholding).

According to a lengthy assessment study of the QSSP by the firm SECOR Inc. of Montreal (1986), seven years after the program was introduced, "Quebec's relative situation has improved from all points of view" (p.i).

- Quebec's firms had significantly reduced their debt level in comparison with their Ontario competitors (p.11);
- The additional fiscal load on Quebec's taxpayers, compared to Ontario, had been reduced on average by 15% since 1983 thanks to the QSSP (p.5);
- The shareholding rate among Quebecers had more than doubled between 1977 and 1985, and was approaching the Ontario rate (pp. 12-16).

In brief, although disparities still existed in Ontario's favour, they had been considerably reduced by the introduction of the QSSP.

One of the main objectives of the program (which helped considerably in establishing the statistical analysis context of this research, set out in chapters 4, 5, 6 and 7) is clearly the progressive use of common share financing by Quebec-based SMBs.

This objective is justified by the economic benefits associated with healthy capitalization.

The SECOR inquiry among all firms issuing QSSP stocks - firms with \$25 million or less in assets at the time of registration - indicated that at least 80%, and probably more, of respondent firms had a debt ratio higher than the industry average before obtaining QSSP funding, but only 45% were in the same position at the time of the inquiry in 1986. The differential compared with the average ratio had also dropped: before their first QSSP issue, 52% of the firms had a debt ratio in excess of 25% of the industry average, compared with only 17% in 1986 (pp. 34-36).

In November 1988, the publication *Canadian Business*, a Toronto-based magazine, also spoke of the entrepreneurial wave that has washed over Quebec since the early 1980s. It revealed that half of the fifty firms having the highest growth rate in Canada were Quebec-based. Of the 25 others, 12 were in Ontario, 7 in Alberta and 6 in British Columbia. According to another article "... this industrial harvest had been sown at the beginning of the 1970s ... and made possible by the creation of the QSSPs" (Canadian Press, 1988).

Mr. Riverin, the current Montreal Stock Exchange President, went beyond the spirit of this statement two years later, when he said that "the QSSP has generated an injection of new money into Quebec's economy and has fostered the emergence of a new generation of entrepreneurs" (Bérubé, 1990: 16).

In more than 10 years of existence, the program has brought an influx of some \$6 billion in the form of permanent capital, half of which has gone into growing SMBs.

According to Riverin, "this capital has allowed QSSP firms to obtain \$18 billion in additional funding, increasing the amount of new money injected into our economy to \$24 billion" (Bérubé, 1990: 16).

In conclusion, the quantifiable financial and economic effects of QSSPs on dynamic SMBs which went public are well-known. This research adds to the knowledge by posing questions on the more qualitative aspects ... and, just as important, on the factors that led these firms to seek public financing, together with the impact of the decision on the owner-manager, his firm and its management, and on the firm's external status.

3.4 Conclusion

Governments in Quebec, Ontario and the other provinces have all encouraged small business expansion through public funding and fostered improved access to capital by dynamic firms through a variety of programs.

The 1981-82 recession highlighted the fragility of this important economic sector. Firms funded mainly by loans and often having a high debt level were hard hit by the exorbitant short-term cost of money (Commission québécoise sur la capitalisation des entreprises, 1984; Economic Council of Canada, 1982).

As a result, the governments had to intervene and support dynamic SMBs in their search for the capital they needed.

This was precisely what the Government of Quebec was aiming to do when it introduced the QSSP scheme to subsidize a substantial part of the fixed costs of portfolio preparation and to facilitate stock exchange listing for growing firms with less than \$25 million in assets and less than 200 employees.

This program, together with other public and private initiatives and the economic recovery in the spring of 1983, quickly breathed remarkable new life into the QSSP program, created in 1978. The success of the programs, and their financial or other performance, was striking, right up to the stock market crash of October 1987. These benefits have been individually assessed and praised from a quantitative and economic point of view many times (see SECOR, 1986, 1988; and various editorials in *La Presse* and other daily newspapers, and in *La Presse d'affaires*).

Despite the apparent success of programs such as the QSSP, some researchers have questioned the logic underlying them. Moussally (1986) declared that firms going under during the recession would have done so anyway, sooner or later, because they were unable

to face the competition of an increasingly specialized and competitive global market. This suggests that access to stock funding sources may not be the only important factor.

According to Guertin (1984), the inquiry commissions failed to recognize that the reason for small business bankruptcies and their dependence on loan financing perhaps lay more in the quality of their decisions and management in the availability of outside funding.

In addition, there are inconsistencies in the data used in the public reports. For example, the Economic Council of Canada explicitly admitted that SMBs were very different in terms of profitability and financial strength. The data also reveal that a fairly considerable portion of funding comes in fact from private investment.

It can, therefore, be said that an entrepreneur's decision to issue or not to issue public stock may not only be a question of financial structure, and that a conclusion based on overall financial data may hinder a deeper understanding of the complexity of this decision.

Chapter 4

PUBLICLY OR PRIVATELY-FINANCED SMBs: PROFILES AND COMPARISONS

4.0 Introduction

Many owners of growing small firms dream of stock market listing. Our data on the situation in Quebec show that, in the summer of 1987, 61.3% believed their firm would eventually be listed.¹

This figure is comparable with the 66.7% of private firm owners who previously had the same dream, but for whom the dream had since become a reality, mainly thanks to the QSSP program.²

The aim of this chapter is to throw some light on the phenomenon of public financing for growing small firms, a phenomenon that has left its mark on Quebec since 1983. The crucial question is as follows: What factors guide the decision of an owner of a growing small firm to use stock market financing, and how does the importance of these same factors vary for owners who chose other methods of funding? The answers to this question had never, until now, been empirically validated - or at least, not in the same way.

¹ A sample of 173 privately-financed firms with a net value between \$1 million and \$12.5 million (see Appendix 1).

² According to our sample, 33.3% of firms currently listed on the Montréal Stock Exchange did not believe that "one day their firm would be listed", which in itself would be an interesting research topic.

Based on the model presented in the first chapter, the decision of an entrepreneur to use stock market financing can be evaluated based on three main categories of variables: those related to the entrepreneur himself, those related to his firm and those related to the firm's financial environment.

The specific aim of this chapter is therefore to verify and empirically confirm the existence of links between the various attributes of the model, and to assess their relative importance according to the three categories of firms, as follows:

1. Publicly-financed firms, or "public" firms, that is, private firms that chose to enter the stock market when the opportunity presented itself.
2. "Open-private" firms, that is, privately-financed firms that are nevertheless open to the idea of stock exchange listing, and that would, in principle, be able to do so.
3. "Closed-private" firms, that is, privately-financed firms that reject the idea of stock exchange listing, despite having the potential for it.

If "public" firms provide a model for other non-public firms that aim to obtain public financing in the future, the attributes of these two types of firms would normally tend to be similar.

This probability led to the adoption of the following three postulates as basic hypotheses of the research:

1. The attributes of the three enterprise populations studied ("public", "open-private" and "closed-private") are different and can be identified.
2. The attributes of "open-private" firms and those of "public" firms are similar.
3. The attributes of "closed-private" firms resemble those of "open-private" firms more closely than those of "public" firms.

These three hypotheses will be examined on the basis of the three components of the model:

- the individual attributes of the owners;
- the attributes of the firm;
- the attributes of the environment.

A fourth section of the chapter will deal with the similarities and differences identified between firms in Quebec and those in Ontario and the rest of Canada.

4.1 Personal attributes of owners and decision to go public

In the literature survey, it became clear that very little research has been done on possible links between personal factors and the decision to use public financing. What has been done tends to show that owners likely to be more interested in public financing had either the *owner/manager* profile (Laufer, 1974) or, more relevantly, the *promoter* profile (Knight, 1983). The authors all agree with de Vries (1977) and Gasse (1981, 1982) that the fear of reduced autonomy and control may also play an important role in the entrepreneur's decision to seek public financing.

In this section, possible links will be sought between the owner's personality and his position vis-à-vis public financing.

TABLE 4.1

PERSONAL ATTRIBUTES OF SMB OWNER-MANAGERS QUEBEC

Personal variables	Categories		
	Public firms (N=69)	Open-private firms (N=106)	Closed-private firms (N=66)
Sex: male*	98.6%	99.1%	98.5%
Average age	43.1 years	45.4 years	47 years
University education	79.7%	58.4%	39%
Additional training*	58%	56.2%	46.9%
Number of professional associations*	2.26	2.54	2
Number of years at the head of the firm	8.3 years	12.1 years	15.1 years
(*) Not significant at 95%			

More precisely, the following personal criteria will be examined in relation to the decision to use public financing: (1) sex; (2) age; (3) education; (4) management training; (5) membership of professional associations; and (6) number of years at the head of the firm.

The results are shown in Table 4.1.

4.1.1 Common attributes: sex, additional management training, membership of professional associations

Table 4.1 shows that, whatever category the firm falls into, the owners are almost all male, have mostly taken at least one or two additional courses in management after their full-time education, and, on average, belong to two professional associations.

TABLE 4.2
AGE GROUPS ACCORDING TO ENTERPRISE CATEGORY
QUEBEC (%) (1)

Category	Age groups			
	< 34	35-44	45-54	> 55
Public firms N=67	10.4	47.8	38.8	3.0
Open-private firms N=103	12.6	39.8	30.1	17.5
Closed-private firms N=63	9.5	33.3	33.3	23.8
Total population N=233	11.2	40.3	33.5	15.0
(1) Significant above 99%				

4.1.2 Differences: age, education, number of years at the head of the firm

The same table 4.1 also reveals that owners in the three categories differ quite significantly in terms of the following variables: age, university education and the number of years at the head of the firm.

4.1.2.1 Age

Table 4.2 shows that nearly 75% of owners are between 35 and 54 years of age, and, apart from those aged 34 or less, the trend towards public financing is more marked among younger owners: the highest proportion of "public" firms is found in the 35-44 bracket, as is the highest proportion of those wanting to go public eventually. The 55 and over group, accounting for 15% of the total number, clearly illustrates this marked relation between age and enterprise type, since it contains only 3% of "public" firms, compared with 17.5% of "open-private" and 23.8% of "closed-private" firms.

TABLE 4.3
LEVEL OF EDUCATION BY ENTERPRISE GROUP
QUEBEC (%) (1)

Category	Level of education			
	Elementary/ Secondary	College	University (Management)	University (Other)
Public firms N=69	14.5	5.8	52.2	27.5
Open-private firms N=106	27.4	13.2	34.9	24.5

Table 4.3 (cont'd)

Category	Level of education			
	Elementary/ Secondary	College	University (Management)	University (Other)
Closed-private firms N=65	36.9	23.1	27.7	12.3
Total population N=240	26.3	13.8	37.9	22.1

(1) Significant at 95%

4.1.2.2 Education

Not only are the "public" type entrepreneurs younger, but they are also better educated. Table 4.3 shows that 79.9% of "public" firm owners have a university education, compared with 58.4% of owners of "open-private" and 39% of owners of "closed-private" firms.

Table 4.3 also shows the strong relation between the level of education and the propensity to seek public financing. The owners of "public" firms are those with the highest percentage of university degrees in management - 52.5%, compared with 34.9% of owners of "open-private" firms and only 27.7% of owners of "closed-private" firms.

Despite growing recognition of the need for better education to succeed in an increasingly competitive business world, more than a quarter of the entrepreneurs forming the research population, those at the head of Quebec's most promising firms, have only a primary or secondary-level education, and a further 13.8% have only a college education.

4.1.2.3 Number of years at the head of the firm

In addition to being younger and better educated, "public" firm owners have also headed their firms for a shorter period than "private" firm owners. Table 4.1 shows that entrepreneurs who have already sought public financing tend to have led their firms for an average of 8.3 years, compared with 12.1 years for "open-private" firms and 15.8 years for "closed-private" firms.

TABLE 4.4
NUMBER OF YEARS AT THE HEAD OF THE FIRM
BY ENTERPRISE GROUP
QUEBEC (%) (1)

Category	Period			Average (years)
	1-7 years	8-14 years	15+ years	
Public firms N=69	55.1	30.4	14.5	8.3
Open-private firms N=104	37.5	29.2	32.7	12.1
Closed-private firms N=63	31.7	25.4	42.9	15.0
Total population N=23	41.1	28.8	30.1	

(1) Significant at 95%

The more detailed data in Table 4.4 show that there are more entrepreneurs with less experience as the head of their firm (41.4% of the total population). More than half chose stock exchange listing. This table also shows clearly, for the three experience levels, that the choice of public financing is strongly related to a shorter period at the head of the firm.

If we wished to speculate on the reasons for the major differences between the "closed-private" firms and the others, we might be tempted to say that most of the owners of "closed-private" firms took over their firms in the 1960s, when university education was the exception rather than the rule, especially in management, a field that grew in importance mainly in the 1970s.

It is also possible that the attraction of a stock exchange listing is less important for these older, more experienced entrepreneurs than for their younger, less experienced counterparts. However, stock exchange listing could be an interesting option when it comes to succession, since it means an external, objective assessment of the firm's value.

To sum up, owners of "public" type firms seem to be better educated, younger and have fewer years' experience at the head of their firms than their counterparts who hope to go public later. In turn, the latter have attributes that resemble more closely those of "public" firm owners.

4.2 Attributes of Quebec firms and the decision to go public

This second section examines the attributes of firms using public or private financing. It compares "public" firms at the time they go public with other firms that have opted to remain "private". The aim is to validate the first partial hypothesis, namely that the attributes of "public" firms are significantly different from those of privately-financed firms. These comparisons will also reveal whether listed firms have advantages over the others at the time they make the decision to go public.

Three types of enterprise-related attributes will be examined:

1. A first descriptive variable: the age of the firm.
2. Four variables relating to the firm's internal situation:
 - the operational plan;
 - the financial plan;
 - the importance attached to the various enterprise functions;
 - the reasons for using public financing.
3. Finally, two variables relating to the firm's external status:
 - the difficulty of obtaining debt financing;
 - the difficulty of obtaining equity financing.

4.2.1 Age of the Firm

Steinmetz (1974) suggests that a firm that has existed for a certain number of years will have grown to a size that would potentially allow it to seek public financing.

However, Table 4.5, showing the average number of years of existence for sampled firms, and Table 4.6, giving further details of these statistics, indicate very significantly that younger firms are more interested in public financing than older firms, whatever the reasons. This observation is consistent with previous observations in this research on the age of owners.

TABLE 4.5
ATTRIBUTES OF SMALL FIRMS
QUEBEC (%)

Variables	Category		
	Public (1) (N=69)	Open-private(2) (N=106)	Closed-private (2) (N=66)
1. Average age of firm	15.63 years	25.55 years	28.82 years
2. Operational plan developed*:			
. less than 50%	44.1	45.7	56.9
. more than 50%	55.9	54.3	43.1
3. Financial plan developed:			
. less than 50%	33.3	44.8	47.0
. more than 50%	66.7	55.2	53.0
4. Importance attached to various enterprise functions (*): (great and very great)			
. marketing/promotion/sales	80.9	82.9	82.8
. management/strategy	79.1	89.6	82.8
. accounting/finance	73.9	74.3	79.7
. production/manufacturing	63.5	76.5	79.4
. information system	52.5	58.3	61.3
5. Difficulty in obtaining debt financing			
. very easy	32.3	44.8	65.1
. fairly easy	26.2	42.9	31.7
. fairly difficult	27.7	10.5	3.2
. very difficult	13.8	1.9	-

TABLE 4.5 (cont'd)
ATTRIBUTES OF SMALL FIRMS - QUEBEC (%)

Variables	Category		
	Public (1) (N=69)	Open-private(2) (N=106)	Closed-private (2) (N=66)
6. Difficulty in obtaining equity financing			
. very easy	20.0	29.7	41.2
. fairly easy	24.6	42.9	37.3
. fairly difficult	29.2	18.7	19.6
. very difficult	26.2	8.8	2.0
(*) Not significant at 95%			
(1) Before becoming public		(2) At the time of the research	

Although significant differences exist between the age of "public" and "private" firms, the difference between the two "private" subgroups (open or closed) are slight. This could indicate that the age of the firm is not a major factor in the decision to obtain stock market listing.

4.2.2 *The operational and financial plan*

Research by Bird (1973), d'Amboise and Gasse (1984), d'Amboise, Gasse and Bernard (1984) and Lorrain and Dussault (1986) shows that firms must have achieved a certain status, and the entrepreneur a certain level of professional managerial competence, before being able to seek public financing. Empirically, therefore, the operational and financial plan should be more highly developed in "public" firms than in "private" firms, and there should also be a difference between "open-private" firms and "closed-private" firms. Table 4.5 supports this hypothesis, although the differences are not statistically significant.

TABLE 4.6
AGE OF FIRMS - QUEBEC (1)

Category	Age			Average (years)
	1-7 years	8-14 years	15+ years	
Public firms N=69	27.5	40.6	31.9	15.8
Open-private firms N=104	12.3	22.6	65.1	25.3
Closed-private firms N=63	10.9	26.6	62.1	28.2
Total population N=234	16.3	28.9	54.8	

(1) Significant at 95%

These results are consistent with generally accepted financial theories, and in the opinion of the researchers suggest that the development stage of the firm well-developed, operational and financial plan is not, at least in the beginning, a major obstacle to obtaining public financing. In fact, the process of stock exchange listing is likely to bring about improvements.

4.2.3 Importance attributed to various enterprise functions

Logically, the management/strategy function should have precedence when a firm is considering public financing. However, Table 4.5 shows no significant difference in any of the five variables from one category of firm to another. The management/strategy function

obtains the highest percentages overall, but not in "public" firms. The percentages in the two "private" categories are in fact higher than for "public" firms. Therefore, the importance accorded to enterprise functions does not seem to be a reliable indicator of the likelihood of deciding to use public financing.

One attribute that is considered less important by all three populations, and especially by "open-private" firms is : the information system. It will be seen later in the research that this is one of the functions that changes most once the firm is listed.

4.2.4 Difficulty of obtaining debt or equity financing

The basic hypothesis leading to the inclusion of this variable - presumed to be fundamental in the decision process - is that the firms most likely to use public financing would be the most flourishing, dynamic and promising SMBs, those that were well-managed and financed.

As Table 4.5 shows, however, "public" firms, before listing, tended to experience the most difficulty obtaining debt or equity financing. Finding private financing seemed considerably easier for the two "private" categories.

These results raise a fundamental question. "Closed-private" firms are perhaps justified in their reticence towards the idea of public financing, quite simply because they do not need other forms of external financing, since they find it easier (than the other two populations) to obtain debt or equity funding. On the other hand, "open-private" firms also found financing easy, although slightly less so.

In the opinion of the researchers, these results mean that other factors play a more significant role in the entrepreneur's decision to use public financing than availability of private financing.

Clearly, as the basic model suggests (Chapter 1), two other kinds of factors play an important role in the decision to go public: factors related to the attitudes and behaviors of the owner himself, and factors related to the firm's financial environment.

The general conclusions to be drawn from Table 4.5 are that younger firms in a more precarious financial situation in terms of access to external financing are those that will decide to go public. On the other hand, the major differences between the "open-private" and "closed-private" firms are not related to the firm itself, but rather to the attitudes of the entrepreneurs themselves, as was observed in the first section of this Chapter.

TABLE 4.7
REASONS FOR GOING PUBLIC
QUEBEC (%)

	Reasons		Most important reason	
	Public (N=69)	Open-private (N=81)	Public (N=68)	Open-private (N=81)
Acquisitions	53.6	66.7	20.6	30.9
Benefits of QSSP*	40.6	23.5	4.4	3.7
Increasing working capital	37.7	51.9	16.2	21.0
Carrying out an Operational plan	36.2	35.8	16.2	17.3
Improving equipment	30.4	27.2	10.3	8.6
Timing was right*	29.0	14.8	7.4	3.7
Investing in firm's image	23.6	14.8	-	2.5
Investing in R&D	23.2	19.8	1.5	2.5
Succession	18.8	17.3	2.9	3.7
Paying off debt	15.9	6.2	5.9	-

(*) Significant at 95%

4.2.5 *Reasons for using public financing*

Table 4.7 sets out the reasons given by firms for using, or wishing eventually to use, public financing.

As can be seen from the first two columns, both groups attach more or less the same level of importance to the factors, except for the benefits of the QSSP program. "Public" firms accord significantly more importance to this particular factor than "open-private" firms. This is not surprising, since, as revealed in Table 4.5, the latter could more easily obtain external capital, and consequently could well go public without the QSSP. This was not the case for firms that had already gone public.

The other two columns of Table 4.7 show that the most common reasons for going or wanting to go public are the same for "public" and "open-private" firms. The four major reasons, by order of importance, are:

1. to make acquisitions;
2. to increase working capital;
3. to carry out an operational plan;
4. to improve equipment.

Of the ten possibilities considered, "QSSP benefits" comes only in seventh place.

4.3 **Attributes of the environment and the decision to go public**

The basic model described in Chapter 1 suggests that a third type of variable plays an important role in the owner-manager's decision whether or not to use public financing: environment-related factors.

Among these variables, we have chosen to consider those that more directly affect the process of accessing external public capital. The hypothesis was: familiarity with the conditions of access and the services offered by underwriters, the Quebec Securities Commission, the Montreal Stock Exchange and other organizations in the field is higher among entrepreneurs who have gone public and among those wishing to do so, than among those that have decided to remain with private financing, and that the perceived difficulty of the stock market listing process (pre- and post-listing period) is lower among entrepreneurs who have already gone public and among those wishing to do so, than among those who have rejected the idea.

Finally, through both intuition and curiosity, we attempted to discover the extent of the changes that followed the influx of public funds in comparison with the importance accorded by entrepreneurs to the various enterprise functions, together with changes in their perception of the difficulty of obtaining private or equity financing.

TABLE 4.8
ATTRIBUTES OF SMALL BUSINESS ENVIRONMENT
QUEBEC
(GREAT + VERY GREAT) (%)

Environmental variables	Category		
	Public (1) (N=69)	Open-private (2) (N=106)	Closed-private (2) (N=65)
1. Familiarity at the time of the decision to go public or stay private			
. eligibility and benefits - QSSP	50.8	37.5	21.5
. role of an underwriter	36.7	23.1	15.4
. role of Securities Commission	27.5	20.2	13.8
. steps to be taken	24.6	27.9	18.4
. services/underwriters	23.1	17.3	16.9
. eligibility/stock exchange	20.3	13.9	6.2
. services/stock exchange*	14.4	9.9	6.2
2. Difficulty/concern about pre-listing period			
. information from underwriter*	10.4	7.1	21.1
. choice of underwriter*	36.2	42.0	48.3
. information from professional assistance centres	17.9	16.5	31.6
. preparing of Prospectus*	60.9	48.6	66.1
. eligibility/QSSP	20.9	20.8	49.1
. eligibility/stock exchange	15.9	23.0	47.4
3. Concern about post-listing period			
. power sharing	8.6	32.4	66.1
. disclosure of information*	42.7	48.6	55.0

TABLE 4.8 (cont'd)
ATTRIBUTES OF SMALL BUSINESS ENVIRONMENT
QUEBEC
(GREAT + VERY GREAT) (%)

Environmental variables	Category		
	Public (1) (N=69)	Open-private (2) (N=106)	Closed-private (2) (N=65)
4. Criteria for choosing a underwriter			
. reputation of underwriter	8.7	15.7	16.4
. friend's recommendation	11.6	1.0	-
. quality of services	34.8	40.2	47.5
. cost of services	1.4	4.9	4.9
. past success	30.4	30.4	27.9
. offices in Quebec	1.4	2.0	1.6
. offices outside Quebec	1.4	-	-
. others	10.1	5.9	1.6

(*) Not significant at 95%

(1) Before going public

(2) At the time of the research

4.3.1 Familiarity with the conditions of eligibility and the process of public stock offering

In general, Table 4.8 (question 1) shows that "public" and, to a lesser extent, "open-private" firms are more familiar with the eligibility conditions and process of going public than the others. Therefore, owners wanting to use public financing seem to know a good deal about stock market eligibility conditions, the benefits of the QSSP and the role of the underwriter in the listing process.

However, fewer entrepreneurs seem to be familiar with the role of the Commission des valeurs mobilières, the steps to be taken for seeking public financing, the various services offered by brokerage houses and the Montreal Stock Exchange listing criteria. This poor state of knowledge suggests that the organizations in question should critically re-examine their promotional methods, and aim to publicize their role and services much more among firms considering public financing.

4.3.2 *Perceived difficulty or apprehension relating to the pre- and post-listing periods*

When questioned about the perceived difficulty of the steps to be taken to obtain stock exchange listing, respondents in all three groups - as can be seen in Table 4.8 (question 2) - were most concerned about drawing up the required documents and choosing a underwriter. In fact, these two factors obtained a higher percentage rating than the four others in terms of perceived difficulty among "public" and "open-private" firms. Also perceived as a difficulty by the "closed-private" firms was understanding the QSSP and Montreal Stock Exchange listing criteria. These additional concerns could result either from a lack of familiarity with the two processes (as can be seen from their poor knowledge of these factors shown in the previous section) or from their lack of interest in this method of financing, or from a combination of both.

In either case, these entrepreneurs would benefit from more regular and complete publicity and informational programs on the part of underwriters and the Montreal Stock Exchange.

As far as the post-listing period is concerned, as can be seen in Table 4.8 (question 3), between 42% and 55% of entrepreneurs were very worried by the obligation of public firms to disclose information on a frequent and regulated basis.

Other interesting, and less expected, results are concerned with the potential loss of power. "Public" and "open-private" firms which, as is often thought in the business world, should be worried about the loss of power resulting from public financing, are in fact not particularly worried by this prospect - only 8.6% of "public" firms and 32.4% of "open-private" firms expressed concern.

However, the question of potential loss of power seems to worry "closed-private" firms much more (66%). It could, therefore, be an important factor in their decision to reject the idea of public financing.

4.3.3 *Criteria for choosing an underwriter*

As can be seen from Table 4.8, two criteria seem to be more frequently used by entrepreneurs when choosing a underwriter, regardless of the category to which their firm belongs. The criteria of quality of service and past success are at least twice as important as any of the five other factors proposed. In addition, these results are statistically significant.

Of all the factors suggested, those considered least important were recommendation by a friend, the general reputation of the underwriter, the cost of the services or the existence of offices within or outside the province of Quebec.

These results tend to suggest that entrepreneurs attach considerable importance to the opinions of their colleagues whose firms have already gone public and, therefore, who have previously had to choose a underwriter. This seems to be supported by the fact that an estimated 75% of businessmen in public firms in Quebec would, if offered the chance to remake their choice, choose the same underwriter.

The differences expressed by the three groups of entrepreneurs in terms of their knowledge of the stock exchange listing process and their concern about the pre- and post-listing periods are more or less as expected. Those who have already gone public have a better knowledge of the conditions and criteria.

Entrepreneurs who will eventually consider going public also have a good knowledge of the conditions, probably because they have sought more information to help them with their decision. Entrepreneurs whose firms were classified as "closed-private" are the least well-informed, since they are less interested in public financing.

TABLE 4.9
DIFFICULTY IN OBTAINING DEBT OR EQUITY FINANCING
BEFORE AND AFTER LISTING
QUEBEC (%)
(N=69)

Level of difficulty	Debt			Equity		
	Before	After	Difference	Before	After	Difference
- Very easy	32.1	56.6	+14.4	20.0	47.8	+27.8
- Fairly easy	26.2	31.9	+ 5.7	24.6	37.7	+13.1
- Fairly difficult	27.7	5.8	- 21.9	29.2	8.7	- 20.5
- Very difficult	13.8	1.4	- 12.4	26.2	5.8	- 20.4

A question arising from these results is whether the entrepreneurs whose firms are in the "closed-private" category would change their minds if the government and other stock market-based organizations provided better information.

4.3.4 Impact of public financing on access to external financing

One particularly critical factor for firm expansion is undoubtedly how easy it is to obtain external financing. This often depends on the general economic situation and other factors

related to the firm's environment. It seemed relevant to verify whether access to financing could be improved by the fact that financial institutions have a better opinion of listed firms.

Table 4.9 shows clearly the positive impact of stock exchange listing on a firm's access to external debt or equity financing for Quebec small firms registered on the stock market through the QSSP program between 1984 and 1987.

Naturally, a "public" firm can attract investors more easily because of the authenticity and reliability of the information available to eventual lenders or investors. This improved access to external financing also means that "public" firms have a considerable strategic advantage over their "private" competitors at the time of acquisition or other investment. This point is particularly important since these firms experienced the greatest difficulty in obtaining external financing before going public (see Table 4.5).

4.3.5 Impact of public financing on the importance attached to management functions

The hypothesis underlying introduction of this variable, one which is consistent with the opinion of many people involved in the stock market sector, is that the importance attached to the management/strategy function by the owner manager is often a practical (although insufficient) criterion for assessing the firm's maturity, generally perceived as essential for admission to the stock market.

The results of Table 4.10 show that entrepreneurs whose firms have gone public considered the management/strategy function to be extremely important for their firm before embarking on the process; as important, in fact, as the marketing/promotion function. After listing, it can be seen that the importance attached to all enterprise functions, except production/manufacturing, increases.

The most significant change is recorded with respect to the information systems. This is not surprising, considering the need for a "public" firm to implement an information system to support its growth and, essentially, to supply continuous and systematic information to its board of directors, shareholders and other regulatory bodies.

Table 4.10 shows that the chief executives themselves do not, however, seem to devote much of their own time to this function. In fact, the proportion of their daily time allotted to information does not increase significantly, which suggests that they delegate this management task - that is, developing, implementing and updating the firm's information system - to professionals.

If a better-structured information system is associated with increased productivity, the results also suggest a direct link between the "public" nature of the firm and an overall improvement in its management, which in turn means an improved ability to compete in the market place.

While the three functions of management/strategy, marketing/promotion/ sales and accounting/finance tended to increase in importance after going public, the differential was less marked in the case of the information system.

TABLE 4.10
ASSESSMENT OF ENTERPRISE FUNCTIONS
BEFORE AND AFTER LISTING
IN PUBLIC FIRMS IN QUEBEC (%)
(N=69)

Enterprise function	Importance attached to function			Time allotted daily by CEO to function	
	Before	After	Difference	Before	After
Marketing/ promotion/sales	80.9	92.8	+11.9	27.5	26.8
Management/ strategy	79.1	91.3	+12.2	23.8	28.8
Accounting/ finance	73.9	91.3	+17.4	20.2	7.8
Information system	52.5	85.5	+23.0	6.8	9.9
Production/ manufacturing	63.5	57.9	- 5.6	19.6	15.1

Table 4.10 also shows that the entrepreneur becomes more aware of all the management functions, and that the chief executive's daily activities shift from production and finance towards strategic management and marketing. These changes are consistent with the firm's changed status, which presupposes a reorientation towards more systematic management methods. They are also a normal part of the progression of the chief executive himself and his time management towards a schedule focused more on strategic development and the long-term.

4.4 Significant differences between SMBs inside and outside Quebec in terms of the decision to go public

In this fourth section, the impact of the attributes of the entrepreneur, the firm and the financial environment on the decision to use public financing in Quebec is compared with the results obtained from a sample of SMB owners from the rest of Canada.

Both populations are comparable, although firms in the "public" sample from the other provinces are larger based on the asset size than the Quebec firms at the time of "going public". However, firms in the "private" sample from the other provinces had an asset base mainly between \$300 000 and \$1 million, while the asset base of the Quebec firms was between \$1 and \$10 million.

In addition to throwing light on some interesting aspects of the attitudes of SMB owners elsewhere in Canada towards public stock offerings as a way of financing enterprise expansion, this section also validates, for the first time, statistically significant relations between the three categories of variables used to explain the decision to seek public financing by the Quebec sample.

4.4.1 *Personal attributes of owners*

Significant differences between the two samples were obtained for two of the six variables examined. As Table 4.11 shows, these were in terms of the level of education and number of years as the head of the firm. Only a few non-significant differences were found for the sex and average age of the entrepreneurs, additional management training and membership of professional associations. A comparison of these results with the results of Table 4.1 shows that the trend in respect of the personal attributes of SMB owner-managers and the decision to use public financing are the same for Quebec entrepreneurs and the others.

Figure 4.1 shows that the owner-managers of firms in the other provinces are older than owner-managers of comparably-sized firms in Quebec. As was the case for Quebec, the average age of the entrepreneurs in the other provinces is higher for "closed-private" firms than for "open-private" firms, and the lowest average age is found among entrepreneurs in "public" firms. However, this is not statistically significant with respect to the 95% threshold for the sample of firms from the other Canadian provinces.

The separate data for the three categories allow a quick comparison of the age difference between the three groups of entrepreneurs in Quebec and those elsewhere in Canada (mainly Ontario). It is clear that "public" firm chief executives in both populations are younger than "open-private" firm chief executives, who in turn are younger than the chief executives of "closed-private" firms.

There is a statistically-significant difference between the level of education of the two populations. The Quebec population is the better educated of the two, with 60% holding university degrees compared with 47.2% for the others. In addition, the Quebec businessmen generally have a management-related university education, whereas the others tend to

TABLE 4.11
PERSONAL ATTRIBUTES OF SMB OWNER-MANAGERS
REST OF CANADA

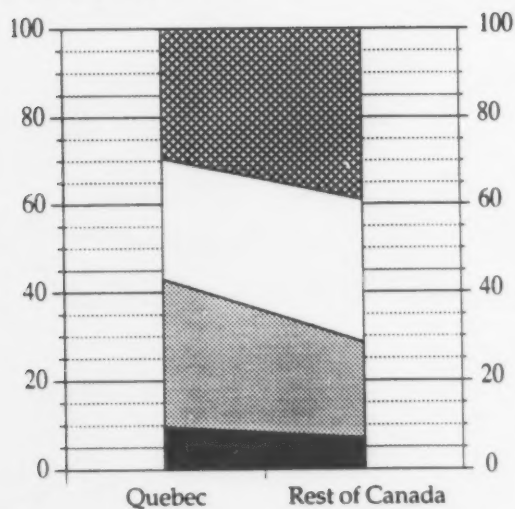
Personal attributes	Category		
	Public firms (N=48)	Open-private firms (N=25)	Closed-private firms (N=85)
Sex - Male*	100%	100%	96.6%
Average age*	48.1 years	49.7 years	52.8 years
University education	64.6%	36.0%	40.9%
Additional training*	50.0%	52.0%	41.4%
Membership of professional associations*	1.5	1.7	1.6
Number of years at the head of the firm	9.86 years	12.04 years	18.07 years

(*) Not significant at 95%

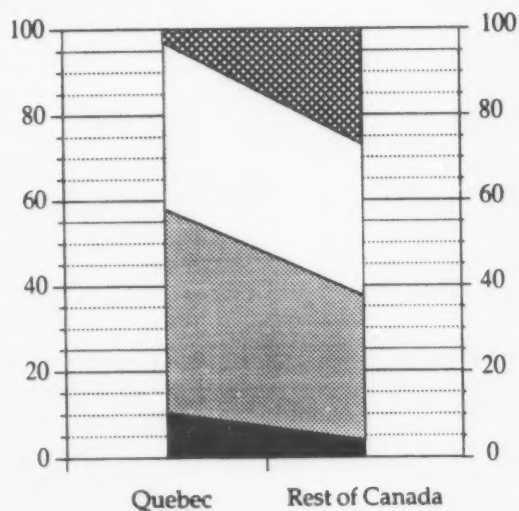
Figure 4.1

COMPARISON OF CEOs BY AGE
QUEBEC AND REST OF CANADA

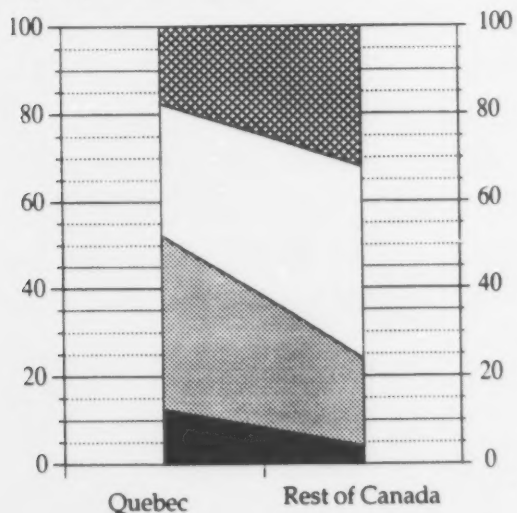
Total population



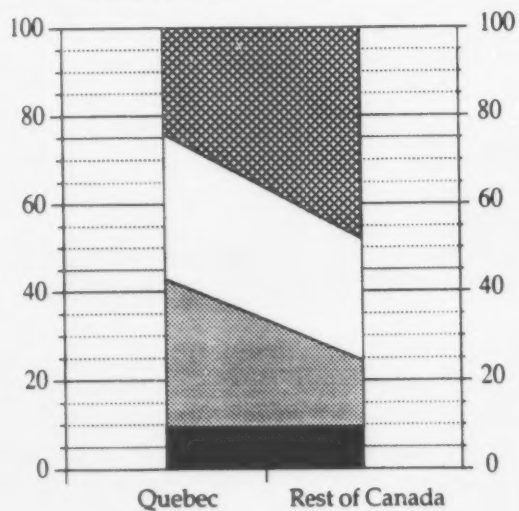
"Public" firms



"Open private" firms



"Closed private" firms



■ 34 and under

■ 35-44

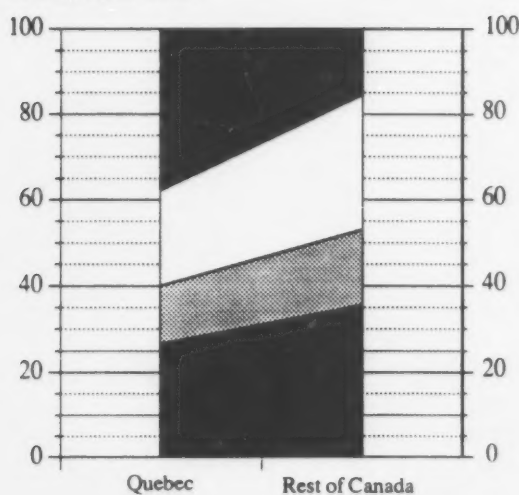
□ 45-55

■ 55 and over

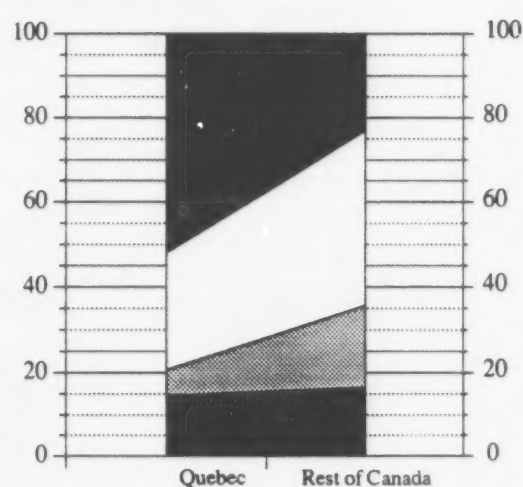
Figure 4.2

COMPARISON OF COMPLETED LEVELS OF EDUCATION
QUEBEC AND REST OF CANADA

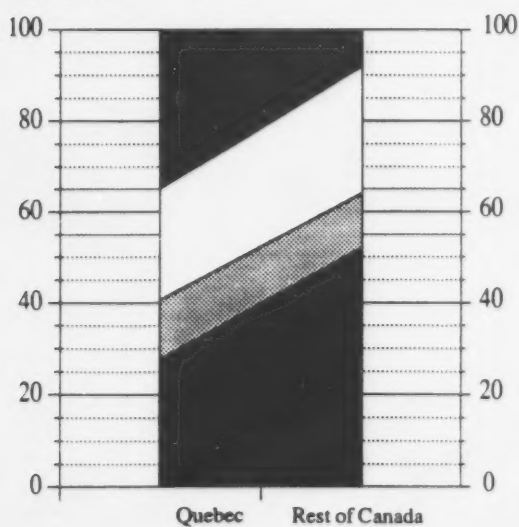
Total population



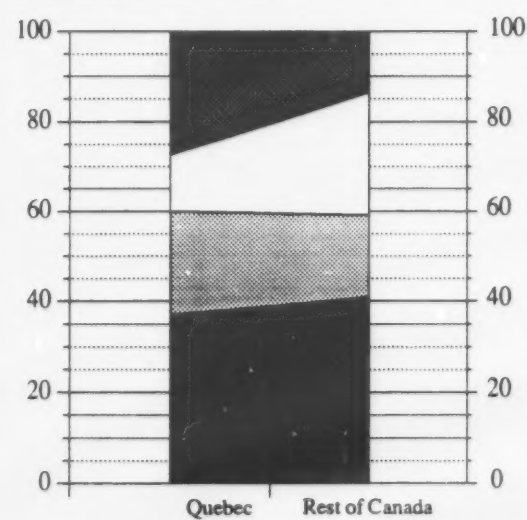
"Public" firms



"Open private" firms



"Closed private" firms



■ Primary and secondary ■ College □ University-others ▨ University-management

have studied in fields other than management. This is surprising at first sight, since the administrative sciences field was neglected to a large extent, right up to the mid-1970s, by French-speaking Quebecers at university. It, therefore, seems clear that the efforts made to catch up, encouraged by the Quebec government and business communities over the last ten years, have brought results and have contributed a good deal to the entrepreneurial spirit underlying Quebec's present remarkable economic development.

Figure 4.2 shows that the percentage of university degree-holders is higher in Quebec for all three groups, but particularly the "public" and "open-private" groups. In addition, entrepreneurs having only a primary or high-school education are more numerous elsewhere in Canada than in Quebec, especially in "open-private" firms, but also in "public" firms.

It can be seen that the level of education of "public" and "private" firm chief executives is very different outside Quebec. "Public" firm chief executives tend to have university degrees, whereas those in "private" firms have only elementary or secondary-level education. However, the level of education for the two "private" groups is fairly similar.

To sum up, Figures 4.1 to 4.4 show that the level of education of chief executives in the three categories varies considerably between the Quebec population and the population from the other Canadian provinces, and also between the categories themselves.

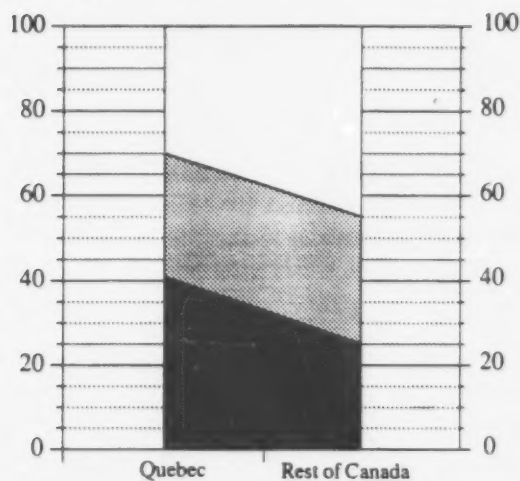
Figure 4.3 presents an analysis of a third variable having a significant effect on the decision to use public financing both in Quebec and elsewhere: the number of years as the head of the firm. In itself, this variable is an approximation of how much the owner is attached to his firm. The hypothesis here is that the decision to use public financing is inversely related to the number of years as the head of the firm, since we believe that greater attachment to his firm and the possibility for independence enjoyed by an owner-manager who has been in place for longer make the decision to move onto the stock market more difficult.

Figure 4.3 shows that, overall, Quebec entrepreneurs have been at the head of their firms for a shorter period than their counterparts elsewhere in Canada. This difference is especially clear in the "public" category, where Quebec has 13% more owners in the 1-7-year category and 12% less in the 15-years-and-over category. The difference is even more marked in the "closed-private" category, where Quebec has 20% more entrepreneurs in the 1-7-year category, and 18% less in the 15-years-and-over category.

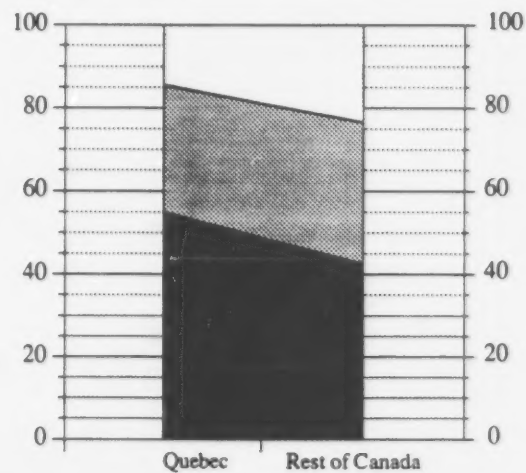
Finally, as was the case for Quebec (see section 1 of this chapter), chief executives of "public" firm outside Quebec have been at the head of their firms for a shorter time than their colleagues in the other two categories. The average is 9.9 years for "public" firm chief executives, compared with 12.1 years for those in "open-private" firms and 18.1 for the others. The figures for Quebec are fairly close to these, although slightly lower, being 8.3, 12.1 and 15.1 years respectively.

Figure 4.3
COMPARISON OF NUMBER OF YEARS
AT THE HEAD OF THE FIRM
QUEBEC AND REST OF CANADA

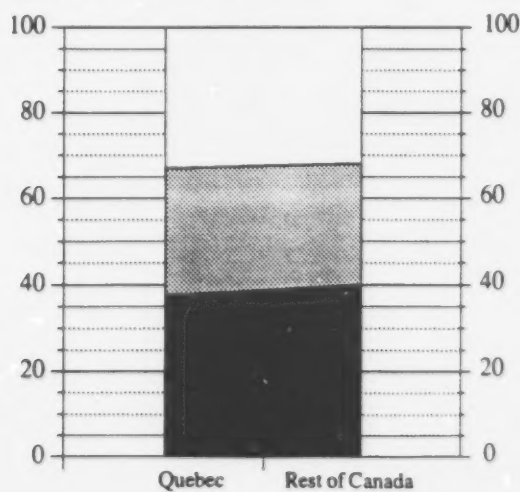
Total population



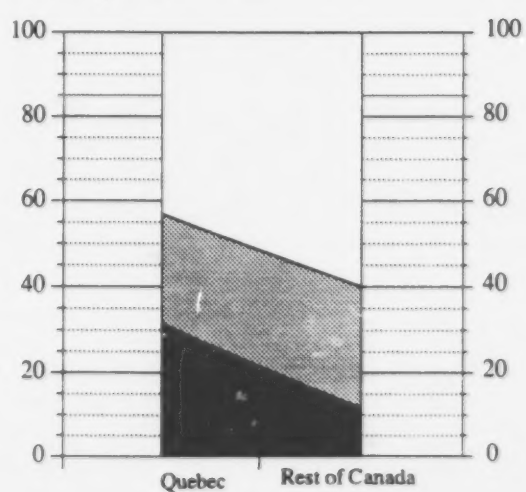
"Public" firms



"Open private" firms



"Closed private" firms



■ 1 - 7 years ■ 8 - 14 years □ 15 or more years

The most interesting conclusions from this section reveal that, as was the case for the Quebec sample, there is a significant statistical correlation between level of education and number of years at the head of the firm, and the decision to go public by owners outside Quebec whose firms satisfy all the listing criteria. These results lead us to believe that chief executives who had taken their firms "public" ("public" firms) generally have a higher level of education and have been at the head of their firm for a shorter period than those who wish to go public but have not yet done so ("open-private" firms). These latter, in turn, have a higher level of education and have been at the head of their firm for a shorter period than those who have rejected the idea of public financing ("closed-private" firms).

Finally, and as was the case for Quebec, there is no significant difference between the three groups in terms of: (i) sex, since more than 95% are men; (ii) additional management training, since around 50% of both populations had followed additional courses; or (iii) membership of professional associations, the average being between 2 and 2.5 for Quebec and 1.5 and 1.7 for the rest of Canada.

More precisely, Quebec entrepreneurs with firms eligible for stock exchange listing are generally younger and better qualified, have taken university-level courses in management, have taken additional management training, belong to slightly more professional associations and have been at the head of their firms for a shorter period than their counterparts in the other Canadian provinces.

4.4.2 *Attributes of the firm*

As far as the attributes of the firms themselves are concerned, significant differences were found between four of the six groups of variables studied among samples of "public", "open-private" and "closed-private" firms outside Quebec. Table 4.12 shows statistically significant differences between the three groups in terms of: age of the firm, the status of the operational and financial plans, and the difficulty of obtaining debt or equity financing. No significant differences were found in terms of the financial plan and the importance attached to the various management functions. A quick comparison with results obtained in Quebec (Table 4.5) shows that the variations are similar for both populations.

In terms of age of the firms, nearly 65% of respondent firms outside Quebec have been in existence for more than 15 years (Figure 4.4). These firms represent not only the majority of the "public" category, but account for three times as many as either of the other two age groups in the two "private" categories. However, in Quebec the percentage of firms 15 years old and over was 10% less; in other words, the Quebec sample contained more younger firms.

Examination of the figures by firm category also reveals a close relation between the age of the firm and the decision to use public financing. The starting hypothesis is therefore confirmed; that is, firms already listed on the stock exchange are younger than firms considering stock exchange listing ("open-private"), which are themselves younger than

TABLE 4.12

ATTRIBUTES OF SMBs - REST OF CANADA (%)

Variables	Category		
	Public (1) (N=48)	Open-private (2) (N=25)	Closed-private (2) (N=88)
1. Average age of firm	19.15 years	24.64 years	30.96 years
2. Operational plan developed:			
. less than 50%	18.8	50.0	46.4
. more than 50%	81.3	50.0	53.5
3. Financial plan developed:			
. less than 50%	29.2	56.1	31.4
. more than 50%	70.9	43.9	68.7
4. Importance attached to various enterprise functions (*): (great and very great)			
. management/strategy	85.5	88.5	79.5
. accounting/finance	80.8	69.2	62.4
. marketing/promotion/sales	76.6	80.0	79.7
. production/manufacturing	60.9	78.3	64.8
. information system	48.9	66.7	45.9
5. Difficulty in obtaining debt financing			
. very easy	13.0	46.2	46.8
. fairly easy	47.8	38.5	42.9
. fairly difficult	26.1	15.4	9.4
. very difficult	13.0	-	1.3

TABLE 4.12 (cont'd)
ATTRIBUTES OF SMBs - REST OF CANADA (%)

Variables	Category		
	Public (1) (N=48)	Open-private (2) (N=25)	Closed-private (2) (N=88)
6. Difficulty in obtaining equity financing			
. very easy	17.8	52.0	40.9
. fairly easy	31.1	28.0	33.3
. fairly difficult	37.8	12.0	19.7
. very difficult	13.3	8.0	6.1

(*) Not significant at 95%

(1) Before becoming public

(2) At the time of the research

firms having rejected the idea ("closed-private"), both in Quebec and in the other Canadian provinces.

The differences revealed by Figure 4.5 with respect to the status of the operational and financial plans give rise to interesting, if hypothetical, comments on the style of management of entrepreneurs in Quebec and in Ontario.

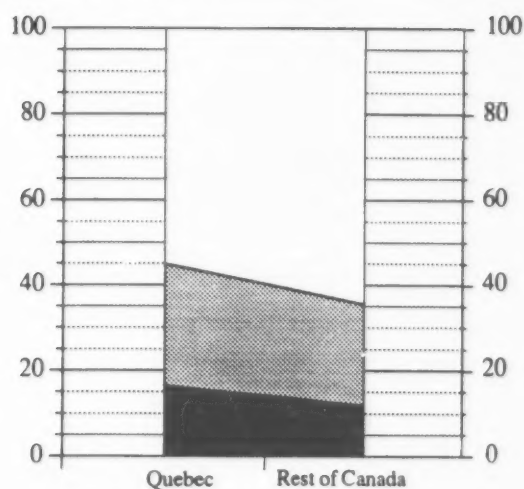
The hypothesis that there is a significant difference in the development stage of the plans between the three groups was not statistically borne out for Quebec, whereas in Ontario, the "public" entrepreneurs seem to have paid more attention to their plans than the two "private" groups.

The differences between public firms in Quebec and Ontario in this respect are quite significant. A total of 44% of Quebec firms, compared with only 18.8% of firms outside Quebec, admitted that their plans were only half developed when they began the stock exchange listing process. These results could, on the one hand, be due to the fact that the Quebec "public" firms were smaller than the others and, although just as young, they devoted less time to this aspect of management in the medium and long-term. On the other hand, they could also indicate a sudden need for funds, for whatever reason, or simply that the firm wanted to take advantage of the QSSP and seize the opportunity to realize their dream of going public.

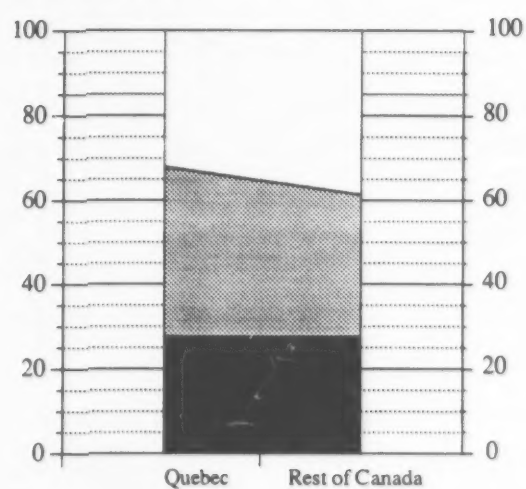
Figure 4.4

COMPARISON OF AGE OF FIRMS
QUEBEC AND REST OF CANADA

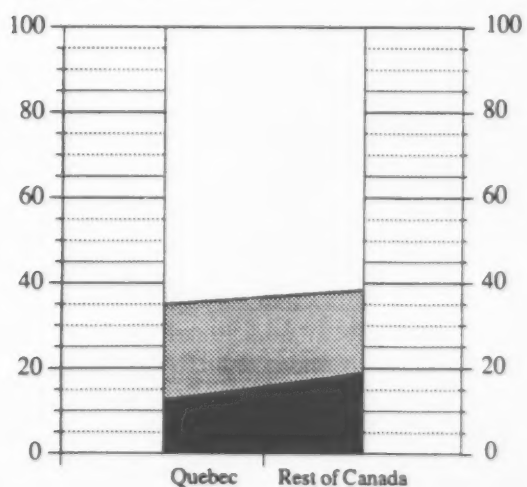
Total population



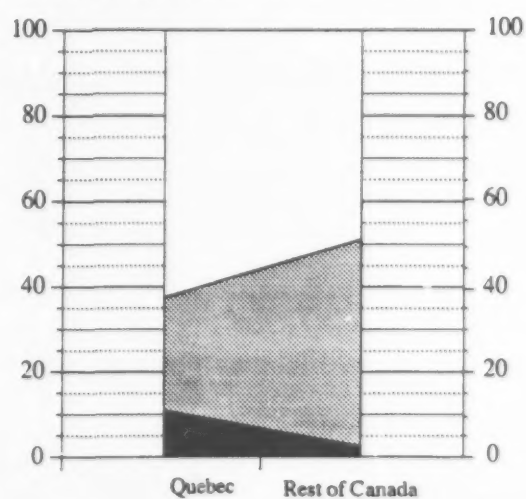
"Public" firms



"Open private" firms



"Closed private" firms

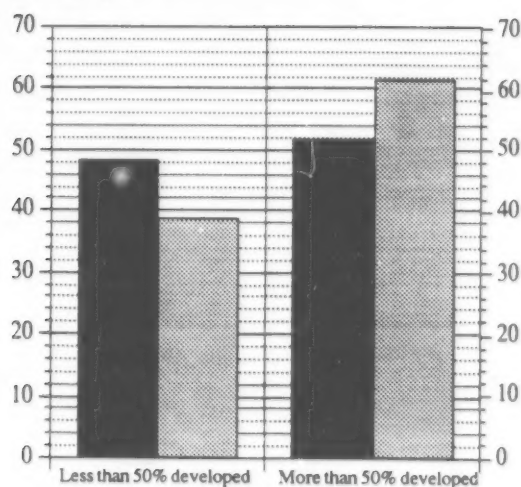


■ 1 - 7 years ■ 8 - 14 years □ 15 or more years

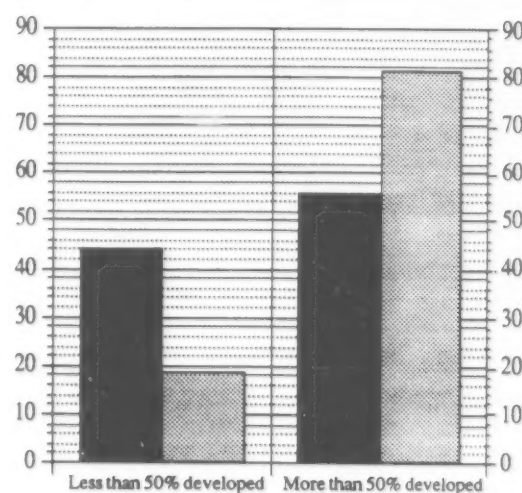
Figure 4.5

COMPARISON OF ENTERPRISE PROJECT DEVELOPMENT
QUEBEC AND REST OF CANADA

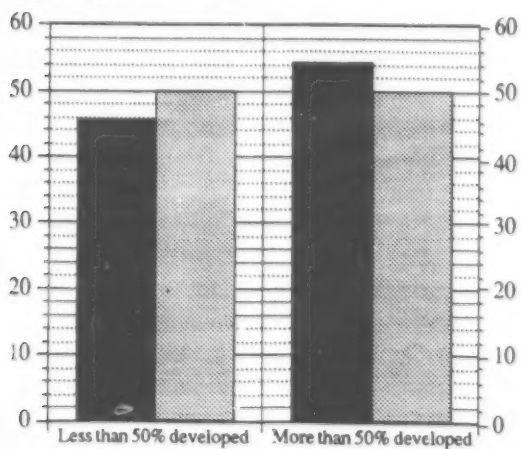
Total population



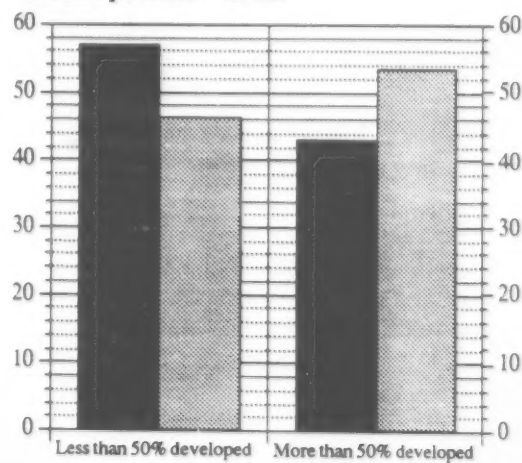
"Public" firms



"Open private" firms



"Closed private" firms



Rest of Canada Quebec

TABLE 4.13
MOST IMPORTANT REASON FOR GOING PUBLIC
REST OF CANADA (%)

	Reasons		Most important reason	
	Public (N=48)	Open-private (N=15)	Public (N=48)	Open-private (N=15)
Increasing working capital	47.9	40.0	33.0	26.7
Carrying out an Operational plan	43.8	20.0	16.7	13.3
Time was right*	33.3	6.7	12.5	-
Acquisitions	31.3	60.0	8.5	13.3
Paying off debt	31.3	6.7	6.3	6.7
Improving equipment	27.1	26.7	10.4	6.7
Investing in firm's image	18.8	26.7	2.1	6.7
Investing in R&D	14.6	26.7	-	6.7
Succession	12.5	6.7	6.3	6.7

(*) Significant at 95%

Tables 4.5 and 4.12 show that a sudden need for funds was not a motive for the Quebec firms since, generally, they did not experience any particular difficulty obtaining outside funding. The importance attached by the Ontario firms to management/strategy is similar to those in Quebec, since the percentages of both populations (tables 4.5 and 4.12) are around 80%, a slight 5% more in Ontario. It seems, for many Quebec firms whose plans were less developed when they decided to go public, that the deciding factor was the QSSP which, as shown in Table 4.7, comes in second place in the list of reasons for seeking public financing.

The "closed-private" firms in Quebec - usually older than the others and experiencing little difficulty obtaining external funding - nevertheless demonstrate a rate some 10% lower than the "closed-private" firms in Ontario as far as development of the operational and financial plans is concerned. This may be explained by a greater lack of concern among Quebec entrepreneurs for this management tool, or by a belief that the past guarantees the future.

Two other variables demonstrated statistically significant differences between the three enterprise categories in Quebec and the rest of Canada.

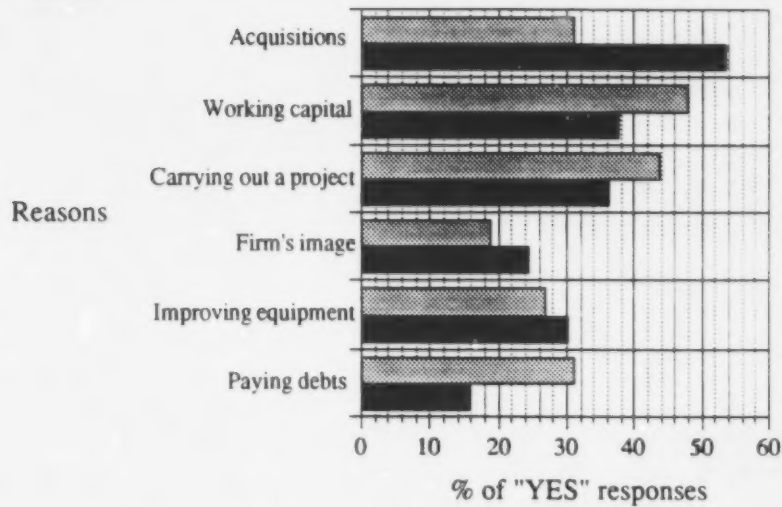
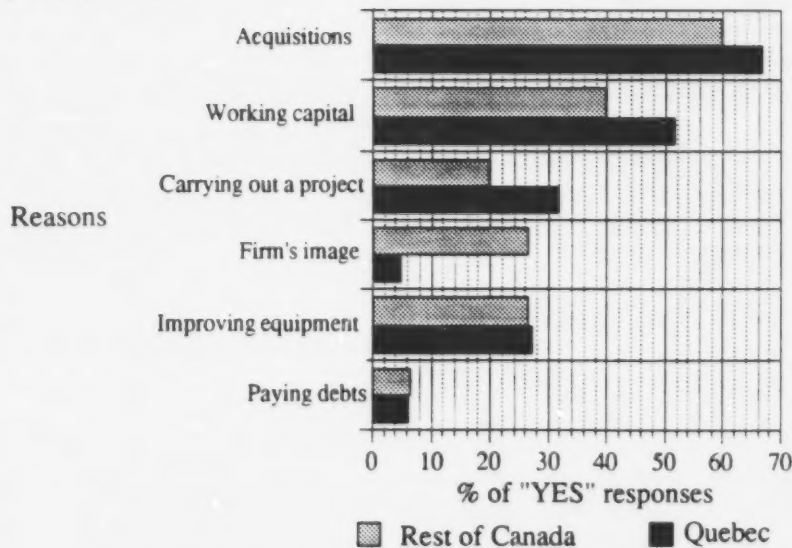
Tables 4.5 and 4.12 show that "public" firms in both Quebec and Ontario found it much more difficult than "private" firms to obtain external debt or equity financing. These differences are very significant, especially between listed Quebec firms with a percentage difficulty of 40% for debt financing and 60% for equity financing, and "closed-private" firms in Quebec, of which only 3.2% had difficulty obtaining this kind of financing. Although the difference in the Ontario figures is slightly lower, the trend is nevertheless the same.

Finally, a comparison between Tables 4.7 and 4.13, as shown in Figure 4.6, reveals that the main reasons for using public financing are the same in Quebec and in the rest of Canada (except for the QSSP, which does not exist in Ontario), for both "public" and "open-private" firms. The major reasons, by order of importance, are: acquisitions, increasing working capital, carrying out a project and feeling that it was the right time to go public, which is in fact the only one of the first four reasons mentioned by public firms that was not also mentioned by "open-private" firms.

Interesting differences exist in terms of the other reasons for public funding. In Quebec, firms already listed on the stock market mentioned the wish to benefit from the QSSP: for them, this comes in second place overall, while it comes in only fifth place for "open-private" firms, which attach much less importance to it.

As shown in Figure 4.6, the most important contrasts between Quebec and Ontario "public" firms in terms of motivating factors are the importance of acquisitions, increasing working capital and payment of debt. This can be explained by the fact that the QSSP firms in Quebec, being younger and smaller, were, perhaps, more tempted at the time of going public by acquisitions, improvement of equipment and installations and by the better

Diagramme 4.6

COMPARISON OF REASONS FOR GOING PUBLIC¹
QUEBEC AND REST OF CANADA**"Public" firms****"Open private" firms**

¹Taking advantage of the QSSP was mentioned by 40.6% of "public" firms in Quebec and only 23.5% of "open private" firms in the province. The program does not exist elsewhere in Canada.

image resulting from their new status than by increased working capital or payment of debt, factors that seem to be more important among "public" firms elsewhere in Canada. On the other hand, according to Figure 4.6, firms both in Quebec and the rest of Canada wishing to go public seem to give similar reasons.

To sum up, the link between the attributes of the firm and the decision to go public confirms the importance of the following variables on the decision: age of the firm, the extent to which the operational and financial plans are developed and access to other sources of external funding. Although the links identified between the reasons for going public given by "public" and "open-private" firms in Quebec and Ontario are not statistically significant, nevertheless they confirm the importance of acquisitions, increases in working capital and carrying out specific projects.

4.4.3 Attributes of the SMB environment

As far as environmental factors are concerned, significant differences between the three enterprise groups were found in the sample from the rest of Canada in terms of familiarity with conditions and the process of admission and the concern about the pre- and post listing periods.

Table 4.14 shows that Ontario entrepreneurs in "public" firms were more familiar with the various stages in the stock exchange listing process than entrepreneurs in "open-private" firms who, in turn, were more familiar with these aspects than entrepreneurs in "closed-private" firms.

These results are comparable with results obtained from the Quebec sample, which also revealed statistically significant differences. Apart from QSSP eligibility conditions and the advantages of this particular program in Quebec, Table 4.8 shows that Quebec entrepreneurs have an acceptable level of knowledge - although less so than their Ontario colleagues - of the role of the underwriter, the role of the Commission des valeurs mobilières and the steps to be taken to obtain stock exchange listing. Stock market eligibility conditions and the services offered to firms by the stock market are the least well-known factors for both groups of entrepreneurs and for all three categories of firms, especially "private" firms.

To sum up, while the decision to use public financing is based partly on the entrepreneurs' knowledge of the conditions for admission and the process to be followed, it seems vital for the organizations involved to provide more and better information to potentially-interested entrepreneurs.

A second environmental factor that has an impact on the decision to use public financing is the level of concern about the pre- and post-listing periods.

TABLE 4.14
ATTRIBUTES OF SMALL BUSINESS ENVIRONMENT
REST OF CANADA
(GREAT + VERY GREAT) (%)

Environmental variables	Category		
	Public (1) (N=48)	Open-private (2) (N=26)	Closed-private (2) (N=81)
1. Familiarity at the time of the decision to go public or stay private			
. steps to be taken	43.8	23.0	8.6
. services/underwriter	38.3	15.4	8.6
. role of underwriter	45.7	19.9	8.6
. role of Securities Commission	29.2	4.0	3.7
. eligibility/stock exchange	27.1	15.4	2.5
. services/stock exchange*	14.6	11.5	1.3
2. Difficulty/concern about pre-listing period			
. information from underwriter	10.4	25.0	38.0
. choice of underwriter	27.1	52.2	60.3
. information from professional assistance centres	10.4	26.0	40.0
. preparing of prospectus*	50.0	54.2	55.4
. eligibility/stock exchange	14.6	45.9	57.2
. Securities Commission regulations*	25.0	39.1	41.8
3. Concern about post-listing period			
. power sharing	6.3	28.0	45.1
. disclosure of information*	23.0	52.1	62.9

TABLE 4.14 (cont'd)
ATTRIBUTES OF SMALL BUSINESS ENVIRONMENT
REST OF CANADA
(GREAT + VERY GREAT) (%)

Environmental variables	Category		
	Public (1) (N=48)	Open-private (2) (N=26)	Closed-private (2) (N=81)
4. Criteria for choosing a underwriter			
. reputation of underwriter	31.3	25.0	41.1
. friend's recommendation	-	4.2	1.4
. quality of services	25.0	25.0	28.8
. cost of services	2.1	-	2.7
. past success	35.4	37.5	24.8
. offices in Quebec			
. offices outside Quebec			
. others	6.3	8.3	1.4

(*) Not significant at 95%

(1) Before going public

(2) At the time of the research

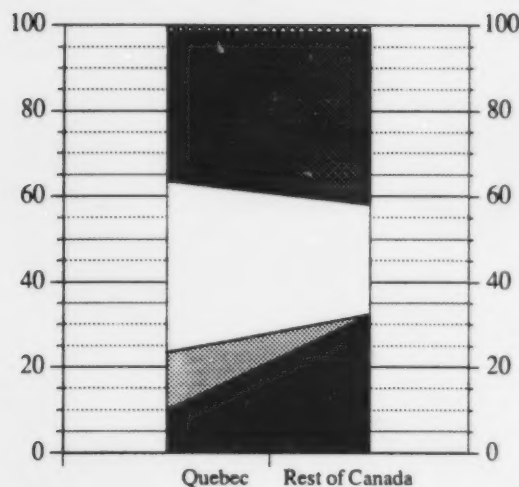
Table 4.14 shows that three aspects of the pre-listing period are particularly worrying for businessmen in the rest of Canada: drawing up the required documents is of concern to 50% of entrepreneurs from all three enterprise categories, followed by the choice of a underwriter and finally, the fear of not being able to satisfy regulatory requirements. These three factors account for the major part of the process.

In Quebec, the same concerns exist, as Table 4.8 shows. However, more entrepreneurs are worried about the need to draw up documentation, and less about the choice of a underwriter.

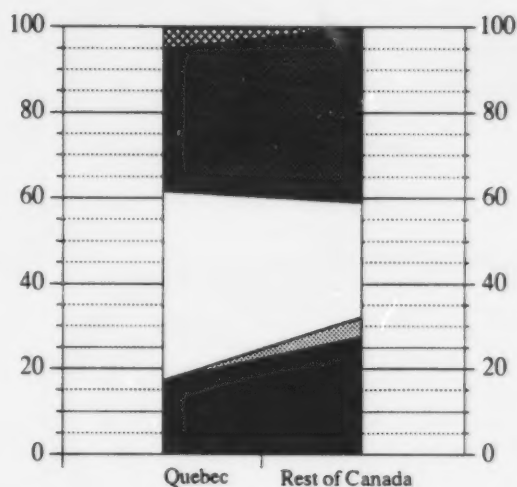
One source of concern about the pre-listing period is the choice of a underwriter to support the entrepreneur in the listing process and to take responsibility for submitting the final documents. Each of the three groups was asked to identify their most important criterion when choosing a underwriter, in the hope of throwing some light on this factor.

Figure 4.7
COMPARISON OF MOST IMPORTANT CRITERIA
WHEN CHOOSING A BROKER
QUEBEC AND REST OF CANADA

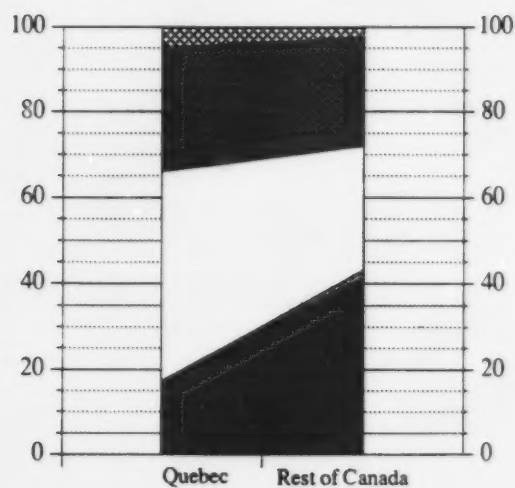
"Public" firms



"Open private" firms



"Closed private" firms



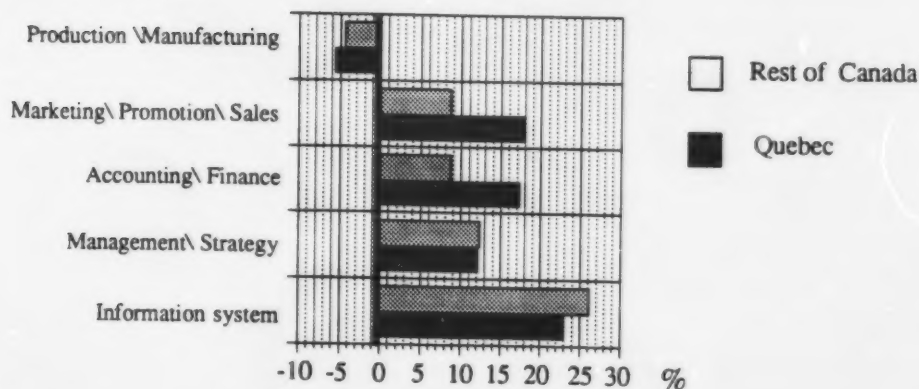
■ Reputation ■ Friend's recommendation □ Quality of service ■ Past success ■ Cost

As was seen in Table 4.8, in Quebec the quality of service offered by the underwriter, together with his track record, were the most important factors, although the response of each of the three groups differed significantly from one element to the next.

Figure 4.7 contains a comparison of the Quebec results with the Ontario results. It can be seen that "public" firms had, as their first or second choice, the track record of the underwriter or the quality of his services, followed by his reputation. The same trend is observed among "open-private" and "closed-private" firms. These results seem to suggest a need for more information on the expertise and experience of underwriters and others involved in the stock market sector in order to reduce apprehension related to the decision to go public.

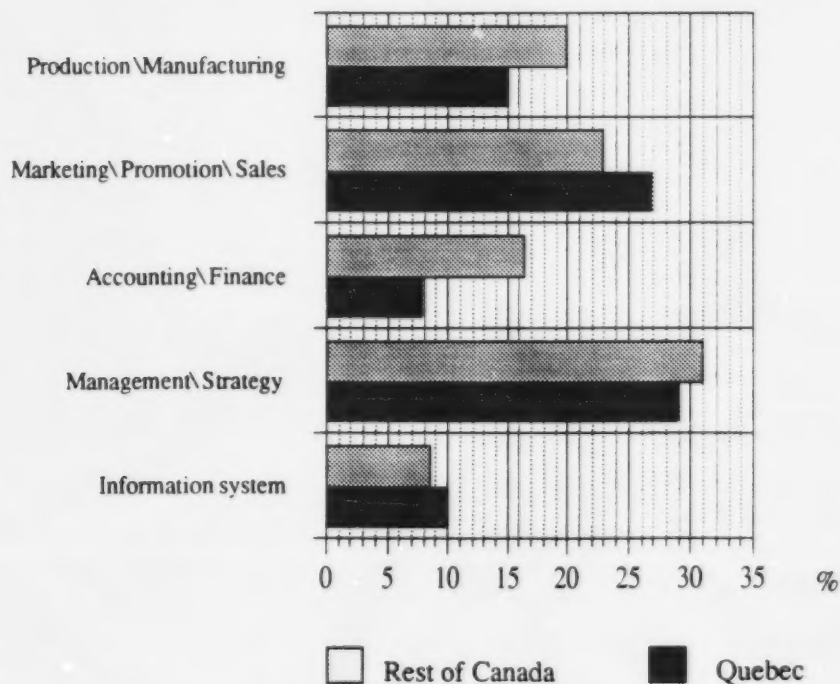
As far as the post-listing period is concerned, being forced to share power with the board of directors and shareholders, together with circulating information on the firm's performances, seem to be clear causes for concern among "closed-private" entrepreneurs in both Quebec and Ontario. Tables 4.8 and 4.14, however, show that the results are significantly different for the three enterprise categories, and that the level of commitment or interest in stock exchange listing reduces the perceived importance of these conditions for "public" and "open-private" firms.

Figure 4.8
CHANGE IN PERCEIVED IMPORTANCE OF
ENTERPRISE FUNCTIONS BEFORE AND AFTER LISTING
QUEBEC AND REST OF CANADA



Tables 4.5 and 4.12 show the importance attached to management functions by Quebec and Ontario entrepreneurs, and the ease of access to external funding. These factors have a substantial impact on the decision to seek public financing. The impact of going public on the various management functions and on access to external funding was also examined. Table 4.10 and Figure 4.8 show that, both in Quebec and the rest of Canada, an influx of public funds has a considerable impact on the importance attached to the enterprise functions, especially the information system, which becomes a major tool for responding to the demands of the firm's new status. The information system becomes of primary importance and, as shown in Figure 4.9, becomes the responsibility of specialists or other managerial staff within the firm, since the chief executive, both in Quebec and the rest of Canada, gives priority in his time management to management/strategy, followed by marketing/promotion/sales, and then production/ manufacturing, accounting/finance and, finally, the information system.

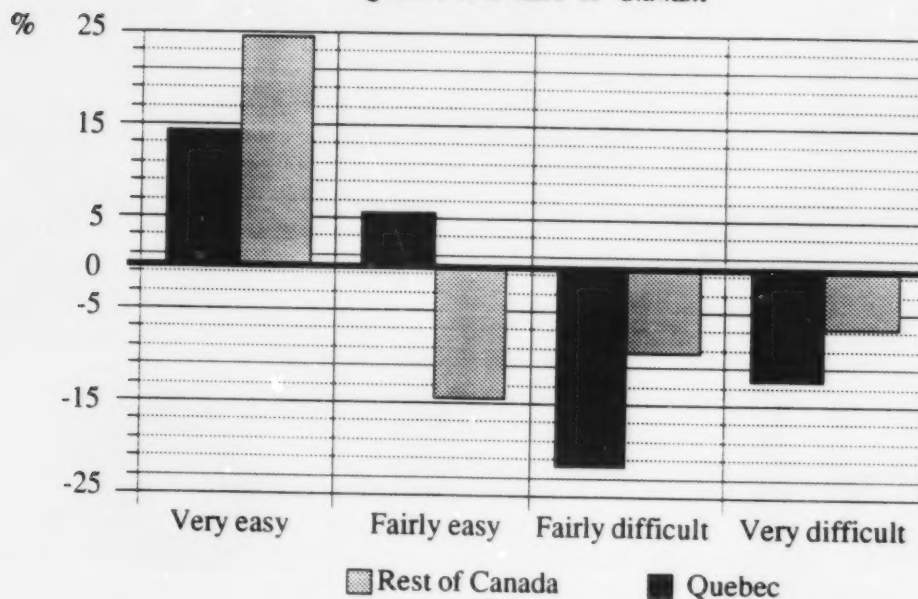
Figure 4.9
COMPARISON OF CEOs DAILY TASK
BEFORE AND AFTER GOING PUBLIC
QUEBEC AND REST OF CANADA



Tables 4.5 and 4.12 show that "public" firms in Quebec and elsewhere experienced more difficulty in obtaining external funding before going public. Figure 4.10 shows the impact of the firm's new status on access to debt financing, and Figure 4.11 on access to equity financing.

The new status of a "public" firm improves its image and its credit in financial circles, so that any previous problems of access to external debt or equity funding seem to be resolved.

Figure 4.10
COMPARISON OF DIFFICULTY IN OBTAINING
DEBT FINANCING AFTER GOING PUBLIC
QUEBEC AND REST OF CANADA



4.5 Conclusion

These results lead us to conclude that, in contrast to their counterparts who choose private funding, owner-managers who opt to go public, both in Quebec and in the rest of Canada, since 1983, show significant differences.

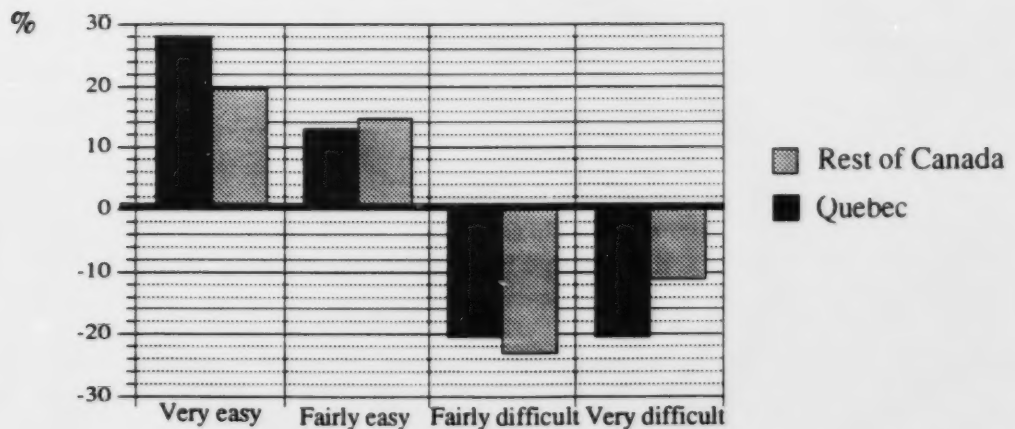
As far as personal attributes are concerned, the chief executives of "public" firms are more likely to have a university education and to have been at the head of their firms for a shorter period than the others. In addition, the average age of entrepreneurs in listed firms is lower in Quebec than in the rest of Canada.

In terms of the attributes of the firm itself, listed firms both in and out of Quebec are significantly younger than unlisted firms. Before obtaining stock exchange listing, these firms found it harder than the others to obtain external debt or equity funding. And, in particular for the rest of Canada, listed firms had a more developed operational and financial plans at the time of listing than unlisted firms.

As far as the attributes of the financial environment are concerned, the results confirm that, both in Quebec and the other Canadian provinces, "public" firms were, at the time they decided to go public, more and better informed about admission criteria, the steps to be taken for listing on the stock exchange, and the general conditions implied by the status of public company. In addition, fewer than 8% of firms who expected to list on the stock exchange were concerned about power sharing after listing, compared with 28% or more of privately-financed firms.

The question that can be asked as a result of these observations is as follows: If the personal attributes of "public" firm owners differ, if "public" firms have different attributes from "private" firms, and third, if there is a difference between what listed and unlisted firms know about the financial environment as such, then research should concentrate on identifying which of these three attribute groups has the most influence on the decision to seek funding by going public.

Figure 4.11
COMPARISON OF DIFFICULTY IN OBTAINING
EQUITY FINANCING AFTER GOING PUBLIC
QUEBEC AND REST OF CANADA



Chapter 5

THE IMPACT OF PUBLIC FINANCING ON SMBs IN QUEBEC AND THE REST OF CANADA

5.0 Introduction

This much-needed research on the reasons for using stock market financing revealed new - or at least hitherto unverified - conclusions. At the same time, it also seemed logical in this study to examine, in depth, the impact of public financing on SMBs in Quebec and the rest of Canada. Therefore, the third part of the research questionnaire, completed by firms that had already gone public, contained a set of questions developed for this purpose. Six kinds of impact were identified; the elements making up each type were determined through research among entrepreneurs and stock market experts. Five of the resulting categories were enterprise-related: structure, labour relations, the decision process, general communications and the firm's status. The sixth was related to the possible changes affecting the owner-manager.

The basic postulate underlying this typology is that a major influx of equity capital from external investors who, as shareholders, obtain often considerable ownership of the firm, has significant spinoffs at three levels:

1. on the firm itself, by the fact of becoming public;
2. on the behavior of the manager-owner of a now-public firm;
3. on the management process of the firm.

The results of the study are described next; first for the Quebec-based firms which went public, followed by a comparison between Quebec-based firms and firms in the rest of Canada.

Overall, Table 5.1 shows that the changes perceived by 69 of the 104 CEOs in Quebec-based firms that went public between 1979 and 1987 were primarily related to the status of the firm, then on the firm's structure, communications in general, the decision process, the entrepreneur himself and, finally, labour relations within the firm.

TABLE 5.1
OVERALL PERCEPTION OF THE IMPACT OF PUBLIC
FINANCING ON SMBs IN QUEBEC (%)
(N=69)

Elements	Rank*						Total
	1	2	3	4	5	6	
EXTERNAL DIMENSION							
1. Firm's status	49.2	16.9	15.4	7.7	6.2	4.6	100%
INTERNAL DIMENSION							
2. Restructuring of firm	24.2	25.8	14.5	12.9	11.3	11.3	100%
3. Communication in general	16.7	27.3	22.7	15.2	10.6	7.6	100%
4. Decision process	4.5	15.2	30.3	22.7	22.7	4.5	100%
5. Labour relations	1.6	3.2	4.8	15.9	27	47.6	100%
PERSONAL DIMENSION							
6. CEO himself	3.2	9.5	9.5	22.5	17.5	38.1	100%

(*) 1= greatest change... 6= smallest change

The data confirm a certain polarisation of the impact felt by CEOs after listing. Almost 50% realise first that "the firm seems to enjoy a new status in the eyes of the rest of the world" after going public - a status it did not have before. Another strongly-felt impact mentioned by 47% of the entrepreneurs questioned concerned "changes in management of the firm". This second grouping covers aspects related to restructuring of the firm, its communications, the decision process and labour relations. Finally, a third element, placed at the top of the list by only 3.2% of the CEOs questioned, concerned the owner-manager.

These results suggest that the major reasons for seeking public financing are, in order, improving acquisition capabilities, increasing working capital, carrying out long-term plans or investing in equipment and structures. Therefore, it seems normal that achieving one or more of these objectives would demand considerable changes in terms of internal management. This also explains why 47% of respondents placed this group of factors at the top of the list in terms of the impact of public financing.

The firm's new status is perceived by 50% as being the most important impact of going public. This very high percentage may be due to the fact that going public is in itself a recognized, if not objective, evaluation of the professionalism and quality of the firm's management and its present and future projects. Another clear reason is that there is an increased focus on public companies by specialized and other media among potential investors, the business community and the general public.

The fact that the impact on the owner-manager was the first choice of only 3.2% respondents could mean that personal benefits are not the main goal when public financing is sought - or at least, that CEOs will not admit it. However, the owner-manager's subsequent personal recognition is sure to be much greater because of the associated high profile as the firm's main representative both internally and externally.

5.1.1 Change in the firm's status

CEOs consider that the firm's new status brings with it certain obvious benefits.

As can be seen in Table 5.2 (question 1), the majority agree that the most significant change is an improvement in the firm's image with suppliers, customers, the business community and the general public. In addition, 50% of respondents mentioned that going public was, for them, a way of obtaining an objective evaluation of their firm. We suggest that this increased visibility and credibility may also make it easier to obtain outside debt or equity financing - something which many SMBs found difficult before they went public. All these changes were assessed by the CEOs as being 100% positive.

However, 50% also mentioned a considerable feeling of powerlessness vis-à-vis fluctuations in the firm's listed stock price, since they had little or no influence on this situation. However, only 3% identified this as being the most striking change. Nevertheless, it was felt to be a negative factor by most respondents.

TABLE 5.2
ASSESSMENT OF THE IMPACT OF PUBLIC FINANCING
ON SMBs - QUEBEC (N=69)

	Changes observed (%)(1)	Most striking change (%)(2)
EXTERNAL DIMENSION		
1. Firm's status		
. Improvement in firm's image with suppliers, customers, etc.	85.5	50.7
. Easier to obtain external funding	71.0	30.4
. External evaluation of firm through stock price	50.7	2.9
. Feeling of powerlessness vis-à-vis fluctuations in stock price	50.7	15.9
		100%(2)
. Positive impact		83.6
INTERNAL DIMENSION		
2. Structure		
. Increase in managerial function	79.4	59.1
. Establishment of new divisions	54.4	18.2
. Establishment of new positions and functions	39.7	16.7
. Other		6.0
		100%(2)
. Positive impact		94.1

TABLE 5.2 (cont'd)
ASSESSMENT OF THE IMPACT OF PUBLIC FINANCING
ON SMBs - QUEBEC (N=69)

	Changes observed (%) (1)	Most striking change (%) (2)
3. Communication in general		
. More external communications	98.5	91.2
. Use of external consultant in communication	51.5	2.9
. More internal communications	41.2	1.5
. Hiring of communications specialist	20.6	2.9
. Establishment of a communications or public relations department	10.3	1.5
. Positive impact		100%(2) 89.2
4. Decision making		
. More cumbersome administration	72.5	23.2
. External pressure for short-term profitability	58.0	33.3
. Greater influence of board of directors	58.0	15.9
. More rigorous decision making	55.1	24.6
. Loss of control by owner-manager	10.1	1.4
. Influence of shareholders	10.1	1.4
. Positive impact		100%(2) 58.5

TABLE 5.2 (cont'd)

**ASSESSMENT OF THE IMPACT OF PUBLIC FINANCING
ON SMBs - QUEBEC (N=69)**

	Changes observed (%) (1)	Most striking change (%) (2)
5. Labour relations with employees		
. Increased sense of belonging to firm	81.8	60.0
. Stock purchases for employees	72.7	21.5
. Improved working climate	30.3	4.6
. Increased employee productivity	21.2	3.1
. Higher demands by workers	15.2	10.8
. Lower performance by employees	4.5	0.0
		100%(2)
. Positive impact		89.1
PERSONAL DIMENSION		
6. CEO as an individual		
. Increased personal pride	61.5	20.0
. Greater professional recognition	56.9	18.5
. Feeling of powerlessness vis-à-vis firm's stock price	40.0	18.5
. Higher social status	33.8	9.2
. More interest in work	33.8	12.3
. Less family time	27.7	9.2
. Less time for employees	18.5	1.5
. Less independence	12.3	7.7
. Reduced social benefits	12.3	3.1
		100%(2)
. Positive impact		65.6

(1) Respondents could choose more than one element for each variable.

(2) May be slightly above or below 100% due to rounding.

5.1.2 Changes in management

Table 5.1 also shows that the major changes in terms of management are related to structure, communications, decision-making and labour relations.

As far as structure is concerned, the most often-cited and significant change is in the development of the managerial function (see Table 5.2 - question 2). Logically, this would lead to the creation of specialised positions and tasks and, in time, new departments or divisions. These changes are perceived by 94.1% as being positive - the highest percentage among all categories of changes.

As Table 5.2 (question 3) shows, the structural changes are accompanied by better communication. Naturally, given the firm's new public status, increased external communications are considered to be the most striking change by more than 90% of CEOs. More than 40% also mentioned better internal communications, a factor that was also implicit in the comments of many of those who listed changes in communications structures, either by the arrival of a specialist or the establishment of a communications department. This need to develop internal and external communications may often imply the establishment of an information system and the introduction of computers into the firm.

Communications-related changes are perceived as positive by nearly 90% of respondents, which shows that they attach a good deal of importance to this factor.

The decision process in a public firm is both complex and important. Table 5.2 (question 4) shows that four distinct elements of this process, each related to a specific aspect of the decision process, were identified by 55% or more of respondents as being important changes induced by the firm's new status.

Two of these elements are concerned with management as such: it is perceived by 72.5% of CEOs as being much more cumbersome, although 55.1% also believe that the resulting decision is more rigorous. Interestingly, these two aspects are considered the most striking changes by a similar proportion of respondents: 23.2% and 24.6% respectively.

The other two elements concern the changes in the influence and power structure resulting from public status. It seems normal that outside pressure for short-term profitability is noted by 58% of CEOs, and considered to be the most striking change by the greatest number - 33.3% (see Table 5.2, question 4). The influence of the board of directors, mentioned by 58% of CEOs, was identified as the most striking change by only 15%.

It may be surprising to learn that loss of control by the owner-manager was noted by only 10.1% of CEOs, and considered to be the most striking change by only 1.4%. This result seems to contradict the widely-held belief that public financing considerably reduces the entrepreneur's control of his firm. In fact, the data show that more complex and specialised management resulting from the going public decision need not necessarily imply loss of control over the firm for the owner-manager.

Finally, 70% of the CEOs consider the increased influence of the board of directors to be positive, and 66% consider the decision-making process to be more rigorous. Overall, however, the decision process obtains the lowest positive rating, at 58.5%.

As far as labour relations are concerned, the main factor, and the most striking one for 60% of CEOs, is that the employees, by buying shares or by having access to more information, seem to have an increased sense of belonging to the firm.

This sense of belonging undoubtedly affects the working climate and productivity, as well as employees' demands (see Table 5.2 - question 5). Overall, these changes are perceived as being positive by 89.1% of respondents.

5.1.3 Changes affecting the owner-manager

Table 5.2 (question 6) shows that, of the nine elements used to assess the changes perceived by the owner-manager, the most often mentioned changes, and those considered the most striking, were related to the personal and professional pride in managing a public company.

The price to be paid for this increased personal recognition is, however, a considerable one, in terms of family time and contact with employees, and it also involves the loss of some personal expense account advantages. However, respondent CEOs did not seem to be too concerned by this.

The most worrying factor for entrepreneurs, one which causes them a feeling of powerlessness, is the fact that they cannot influence the value of their firm's shares; and their feeling that the stock price of their firm does not often reflect the real value of either the firm or its management.

Finally, only 12.3% of respondents mentioned reduced autonomy compared with the pre-listing period. This low percentage is worth noting, since it contradicts findings from the literature survey and popular belief to the effect that going public necessarily means loss of autonomy and control for the entrepreneur.

On the whole, changes affecting the owner-manager, with a positive rating of 65.6%, were considered slightly more positive than average.

5.2 The impact of public financing on SMBs in Quebec and the rest of Canada

The aim of the second part of this chapter is to compare the Quebec results on the impact of public financing on firms listed on the Montreal Stock Exchange with results obtained for the rest of Canada for firms listed on the Toronto Stock Exchange.

Conceptually speaking, analysis of the Quebec data enabled us to verify the relevance of the typology developed for the research. As shown below, it also produced hitherto unknown comparative data on the impact of public financing on the status of firms in Quebec and elsewhere in Canada, and on the changes in terms of management and the owner-manager/CEO.

The results will be presented in diagrammatic form to facilitate the comparison between the two groups. This comparison was carried out using three main variables: the perceived impact of the most important change (Figure 5.1), the positive rating for the change perceived as being most striking (Figure 5.2) and a specific examination of each of the six types of changes (Figure 5.3) in the typology.

5.2.1 Comparative impact of the most important change

Figure 5.1 shows that the main impact was felt on the firm's external status, and then internally, and finally on the CEO himself.

Interestingly, the impact felt by Quebec CEOs is very similar to that felt by CEOs from the other Canadian provinces in each of the categories of changes studied. The greatest change, noted by 50% of entrepreneurs both in Quebec and the rest of Canada, is increased visibility and recognition of the firm in the business community and among the general public. The slightly higher - by 5% - impact for firms outside Quebec may perhaps be explained by the higher level of industrialization or the more developed industrial infrastructure, and also by the fact that it is generally considered more difficult to list on the Toronto Stock Exchange than on the Montreal Exchange.

Changes affecting management - particularly structural changes - are the second most important group. Quebec entrepreneurs perceive a greater change: 47%, compared with 42.3% for the rest of Canada. In our opinion, this can partly be explained by the fact that Quebec firms are generally smaller.

Finally, the changes affecting the owner-manager, while much less remarked than the other categories, were mentioned twice as often by respondents outside Quebec. This difference could once again be explained by the fact that it is more difficult to list on the Toronto Stock Exchange, which in turn contributes to a greater feeling of recognition on the part of public company CEOs outside Quebec.

5.2.2 The nature of the impact of public financing

Figure 5.2 shows that the perceived effects of public financing are generally positive both in Quebec and elsewhere in Canada. The management aspect obtains the highest ratings, and the decision-making process the lowest. In our opinion, this result is encouraging and fortunate, since it suggests that the many changes brought about by public financing generally have a beneficial effect on the management of a growing firm.

Figure 5.1

IMPACT OF PUBLIC FINANCING ON SMBs
QUEBEC AND REST OF CANADA

Most important change

External Dimension

Firm's status

Internal Dimension

Restructuration of firm

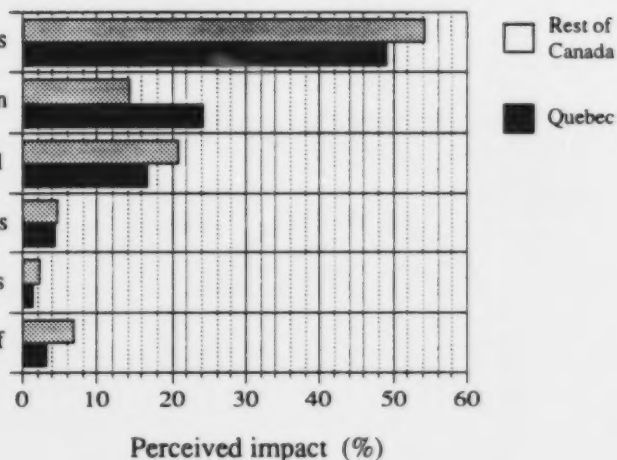
Communication in general

Decision process

Labour relations

Personnal Dimension

CEO himself

**Figure 5.2**

ASSESSMENT OF POSITIVE PERCEPTION
OF IMPACT OF PUBLIC FINANCING
QUEBEC AND REST OF CANADA

Most striking element

External Dimension

Firm's status

Internal Dimension

Restructuration of firm

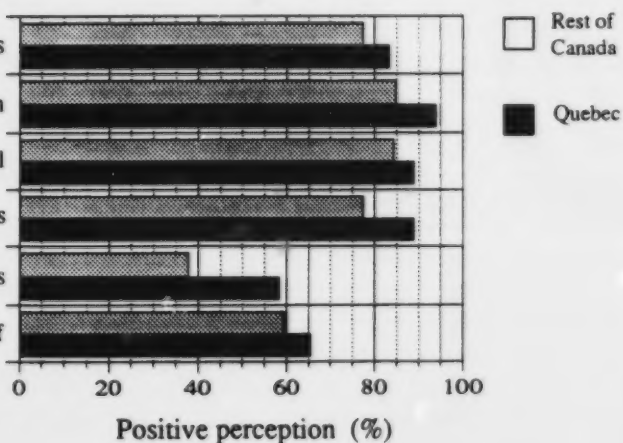
Communication in general

Decision process

Labour relations

Personnal Dimension

CEO himself



The firm's new status comes in second place in the rankings. It helps the firm obtain additional outside funding if necessary, contributes to publicizing the firm both in Canada and abroad, and in some ways confirms its expansion, diversification or acquisition capabilities.

The CEO's personal feeling of success and professional pride is ranked third in terms of positive perception. This is important, since it means that the entrepreneur continues to play a leading role even after his firm goes public, and this feeling is in itself a considerable source of motivation in the face of the new challenges facing him and his firm.

The following sections discuss the impact of each element in greater detail.

5.2.3 Changes related to the firm's status

Figure 5.3 shows that the two most striking changes affecting the firm's status, both in Quebec and the rest of Canada, are a better public image and easier additional external funding. On the other hand, performance and stock price fluctuations are considered more difficult, especially in Quebec, perhaps because the QSSP firms tend to be smaller.

5.2.4 Changes related to management

Two aspects of management-related changes are considered more important: the effects on the structure of the firm and the effects on communications in general. Although each element is dealt with separately, there is undoubtedly an interrelation between them and the other factors.

Figure 5.4 shows that, according to both groups of entrepreneurs, but especially those in Quebec, the impact on the structure of the firm can best be seen through the development of the managerial function. It is interesting to note that, as we said earlier, development of the managerial function seems to lead to the establishment of new divisions in firms in the "rest of Canada" sample - which are generally bigger, older and more mature - and to new jobs and tasks in Quebec firms - which are generally smaller and, therefore, less departmentalized and bureaucratic.

As far as communications are concerned, according to both groups of CEOs, the most striking impact is increased external communications, a phenomenon which is implicit in the firm's new status. Remarkably, the ratings for both groups are comparable, at 95% or more. Increased internal communications are also noted in similar proportions - around 42% - by both groups.

Figure 5.3
IMPACT ON FIRM'S STATUS
QUEBEC AND REST OF CANADA

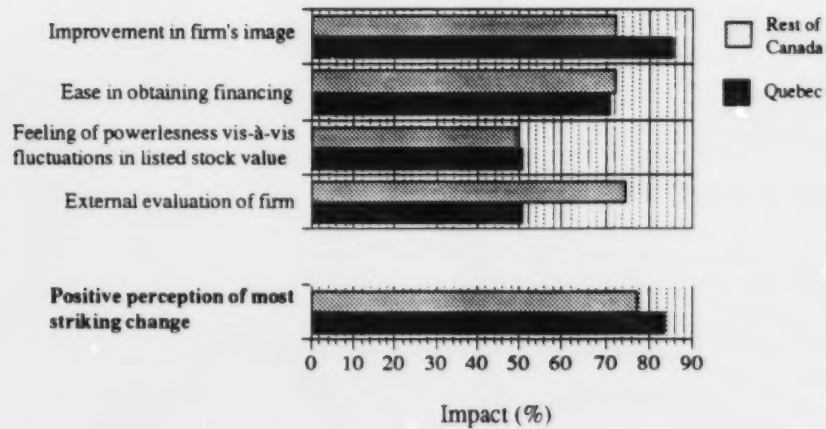


Figure 5.4
IMPACT ON FIRM'S STRUCTURE
QUEBEC AND REST OF CANADA

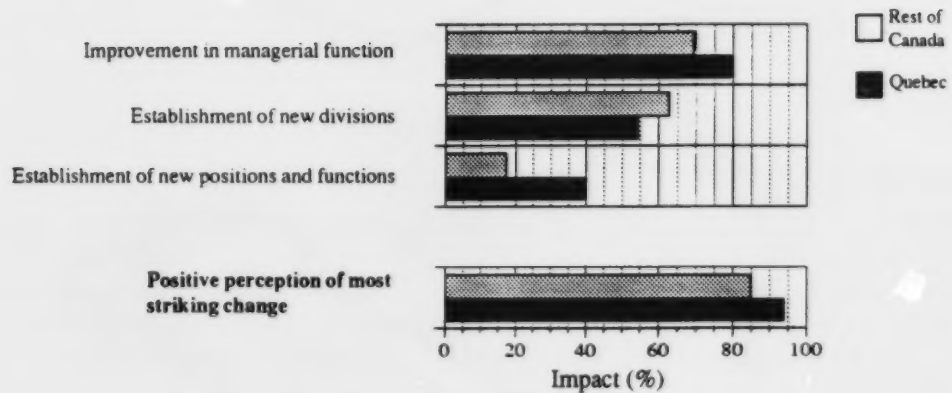


Figure 5.5
IMPACT ON COMMUNICATION IN GENERAL
QUEBEC AND REST OF CANADA

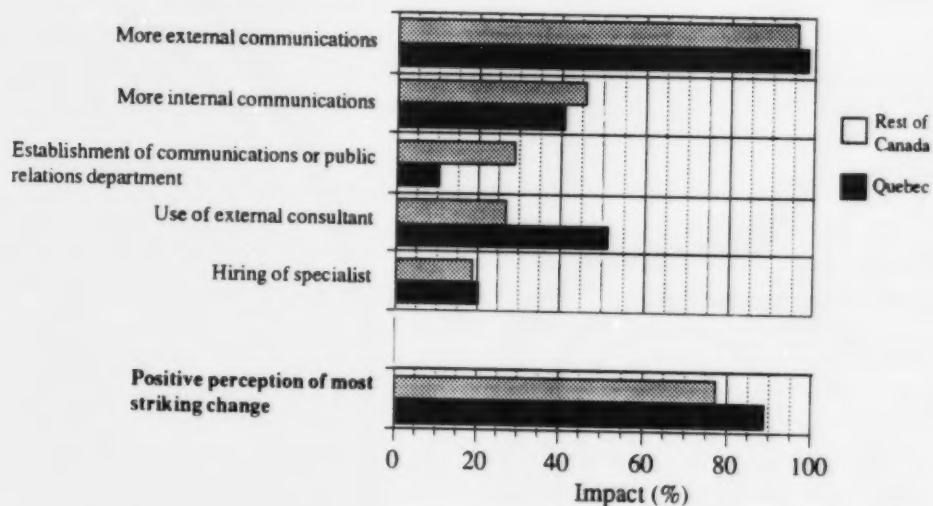
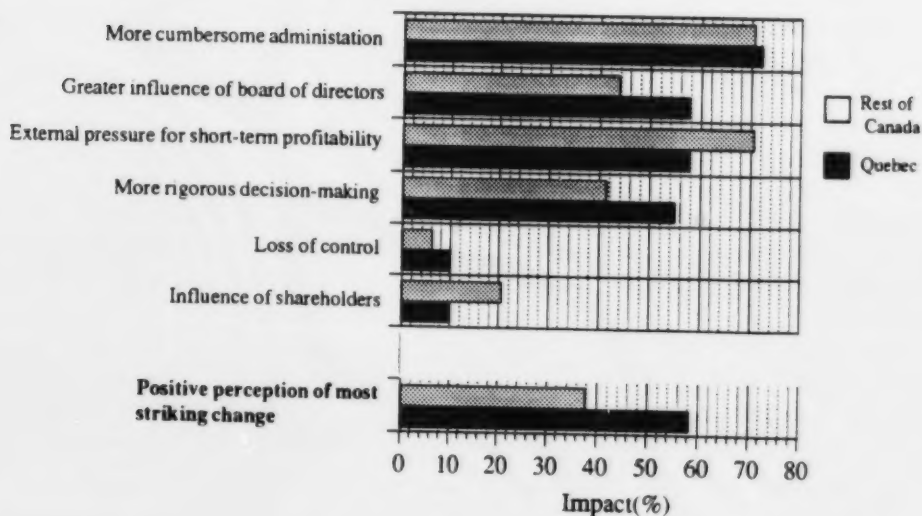


Figure 5.6
IMPACT ON DECISION MAKING
QUEBEC AND REST OF CANADA



However, there are differences in how each group chooses to face this new challenge. In Quebec, firms tend to call in outside consultants, whereas elsewhere they are more likely to set up their own communications or public relations department.

As far as decision-making is concerned, figure 5.6 shows that, for both groups, the administrative apparatus generally becomes more cumbersome, which, together with the increased influence of the board of directors, means more rigorous decision-making. This is particularly so in Quebec.

Figure 5.6 also reveals some interesting and unexpected results. For both groups of entrepreneurs, the influence of shareholders on the decision process is minimal (10% in Quebec, 20% outside Quebec). Therefore, there is no real loss of control by the CEO when his firm goes public. In our opinion, these are two major findings which contradict generally accepted ideas.

Finally, both groups of entrepreneurs - but in particular the group outside Quebec - feel considerable outside pressure for short-term profitability. This is in line with the predictable attitudes of some investor-shareholders, but may mean reduced flexibility in terms of strategy and long-term management.

Finally, as can be seen in Figure 5.7, both groups agree that the impact of public financing on labour relations is most clearly illustrated by an increased sense of belonging among employees. This is widely fostered by employee share purchase programs, especially in Quebec.

The positive rating for this change from both groups is high - 89% in Quebec and 85% in the rest of Canada. Thus, a better working climate and higher productivity are considered important by both groups.

5.2.5 Changes affecting the owner-manager

As far as the impact on the owner-manager is concerned, Figure 5.8 shows that feelings of professional recognition and personal pride are the most noted changes among both groups, but especially in Quebec. However, the social status of CEOs tends to be higher outside Quebec.

CEOs outside Quebec, while having less family time, seem to have more time available for their employees. They also seem to suffer less than their Quebec counterparts from a net reduction in their social benefits or from pressure caused by a feeling of lack of control over their firm's share price.

Figure 5.7
IMPACT ON LABOUR RELATION
QUEBEC AND REST OF CANADA

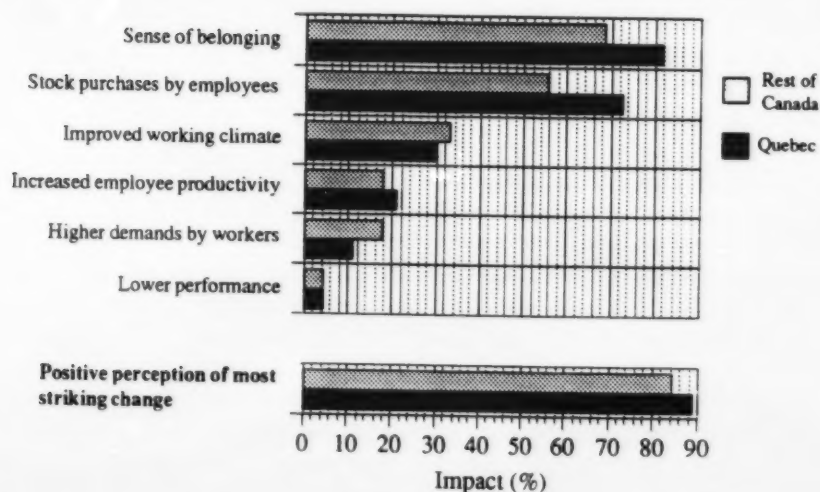
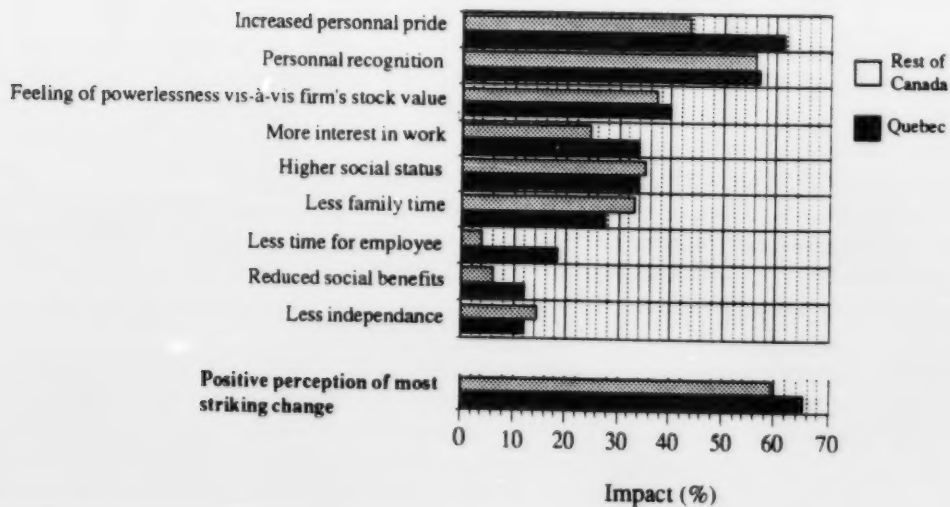


Figure 5.8
IMPACT ON CEO HIMSELF
QUEBEC AND REST OF CANADA



5.3 Conclusions

The results obtained for Quebec and the rest of Canada seem to be consistent. They show clearly that "going public" implies significant changes, first of all in the firm's status, and then in internal management. The owner manager must also come to terms with certain changes when he becomes CEO. The external environment and geographic location of the firm do not affect these changes.

Clearly, the most striking changes are concerned with the firm's status. A listed, publicly-traded firm sees a real improvement in its image among the business community and the general public. Internal and external communications are also significantly increased. Therefore, any entrepreneur considering going public, but particularly those in older, more mature firms, must take into consideration the important needs in terms of information and communication that will result.

The changes also include a considerable increase in administration and development of the managerial function, especially for smaller firms in Quebec.

The impact on employees is also positive. A majority of the CEOs questioned had observed an increased sense of belonging among their employees, especially in Quebec.

The area in which the impact of public financing is felt the least seems to be on the effect on owner-manager. Nevertheless, CEOs of public firms inside and outside Quebec admit to an increased feeling of personal pride and professional recognition, and their social status improves.

CEOs tend to perceive the changes resulting from the process of going public as being very positive, whether they affect the firm's status, its internal management or themselves as individuals.

This research leads to at least two important conclusions. First, going public not only means an immediate and considerable influx of funds, but also a number of significant and positive changes for the firm's internal and external environment and the CEO himself. Consequently, access to public financing can be considered to be a first, and extremely important, step towards growth and maturity.

Second, going public is a very positive experience for Canadian entrepreneurs. The results from both samples studied in this research indicate that this positive experience is felt independent of the geographic location of the firm or the size of the firm.

Chapter 6

INFLUENCE OF GOVERNMENT PROGRAMS ON THE USE OF PUBLIC FINANCING BY SMBs IN QUEBEC

6.0 Introduction

As described briefly in Chapter 3, Quebec government has initiated two main policy initiatives to provide greater equity financing for Quebec-based SMBs: first, the establishment of financial assistance programs to encourage SMBs to opt for public financing; and second - a form of action also taken by the federal government - a more specific policy statement on the amounts and kinds of assistance available to SMBs through crown corporations or government agencies such as the Federal Business Development Bank (FBDB) and the Société de développement industriel (SDI).

The aim of this chapter is, first, using data gathered in Part 4 of the questionnaire sent to public firms, to describe and comment on the influence of Quebec government's stock market access programs, including the QSSP, on the decision by SMBs to use public financing. Its second aim is to examine the reasons given by owner-managers for their choice. The level of satisfaction of firms having opted for public financing will also be examined, and a comparison made between the reasons given for choosing public financing by chief executives in Quebec and in the rest of Canada. Finally, general satisfaction levels will be examined.

6.1 Impact of Quebec government programs to foster stock market access for SMBs

As a result of the Saucier Commission report on business capitalisation, the Quebec government established its stock market access program in 1982, with the aim of making it easier for its dynamic SMBs to move onto the stock market. The program granted financial assistance of as much as \$400,000 to developing corporations with high growth

potential, to offset the often considerable costs related to preparation of documentation and the issue of stocks.

Table 6.1 (section 1) shows that around 40% of the 69 firms making up the Quebec sample had in fact taken advantage of this or other similar programs. Although the percentage is fairly high, nevertheless it also means that 60% of firms went public without any government assistance.

If it is assumed that the 60% corresponds to the percentage of owner-managers who replied "yes, certainly" in Table 6.1 (section 2), then it can also be assumed that only 6% of those who received assistance would have decided against stock exchange listing without it. These results are extremely revealing. In our opinion, they provide a good indication of the motivation and dynamism of Quebec's businessmen with respect to public financing.

As Table 6.1 (section 3) shows, more than 75% of public firms in the sample consider that the QSSP program played an "important" or "very important" role in their decision to go public. However, as can be seen in Table 6.1 (section 4), almost 20% say they would have gone public even without the QSSP, and another 30% think they would "probably" have done so.

These figures, and by extension the spirit of entrepreneurship among chief executives of Quebec's SMBs, are supported by the results set out in Table 4.7, where 40% placed "the benefits of the QSSP" in second place in the list of the ten most common reasons for choosing public financing, but in only seventh place overall (out of ten) in order of importance.

6.2 Reasons for choosing public financing

These well-informed owner-managers consider public financing mainly as a way of getting as much financing as possible at the lowest possible cost (see the percentages in Table 6.1 section 5). However, the particular interest of section 5 lies in the considerable importance (more than 40%) attached by chief executives to benefits of public financing other than financial ones.

As the analysis in Chapter 5 revealed, the benefits of going public on the firm's internal dynamism (generally and among the employees), and in terms of outside visibility, are considered significant, and their positive effects are often underestimated by many owner-managers at the time they make the "going public" decision.

If going public is defined as having access to external equity capital needed to satisfy the firm's growing needs, at a comparatively lower cost than other sources, then the next logical step is to determine the degree of satisfaction associated with that decision.

TABLE 6.1

**INFLUENCE OF GOVERNMENT FINANCIAL ASSISTANCE PROGRAMS
ON THE DECISION TO GO PUBLIC
QUEBEC (N=69) AND OTHER PROVINCES (N=48)**

Variables	Quebec (%)
1. Did you obtain financial assistance from the government to help offset the cost of the initial public offering	
. yes	41.3
. no	58.7
	100.0
2. Would you have gone ahead even without this assistance?	
. yes. certainly	60.4
. yes. probably	16.7
. probably not	16.7
. definitely not	6.3
	100.0
3. What influence did the QSSP have on your decision?	
. none	4.4
. little	4.4
. some	14.7
. great	30.9
. very great	45.6
	100.0

TABLE 6.1 (cont'd)

**INFLUENCE OF GOVERNMENT FINANCIAL ASSISTANCE PROGRAMS
ON THE DECISION TO GO PUBLIC
QUEBEC (N=69) AND OTHER PROVINCES (N=48)**

Variables	Quebec (%)	Rest-of-Canada (%)
4. Would you have gone public without the QSSP?		
. yes. certainly	17.9	
. yes. probably	31.3	
. probably not	35.8	
. definitely not	14.9	
	<u>100.0</u>	
5. Relevance and use of public funding ⁽¹⁾		
. more capital	69.7	89.4
. lower cost funding	57.6	33.3
. greater exposure	45.5	39.6
. new dynamism for firm	50.0	33.3
. greater involvement of employees in firm	42.4	12.5
6. If you had the opportunity to make your decision again. would you still choose public financing?		
. yes. certainly	77.6	77.1
. yes. probably	19.4	18.8
. probably not	3.0	4.1
. definitely not	0.0	0.0
	<u>100.0</u>	<u>100.0</u>

(1) Respondents could choose more than one element for this variable.

6.3 Level of satisfaction among public SMBs in Quebec

The study asked the CEOs of public firms to answer the following question: "You chose public financing for your firm; but if you had the opportunity to reconsider, would you make the same decision again?" Table 6.1 (section 6) shows the results which indicate a very high level of satisfaction with respect to public financing. Almost 78% said they would "certainly" make the same decision in the same context, and another 20% said they would "probably" do so. Only 3% would think twice before going down the same path in comparable circumstances.

In our opinion, these figures demonstrate an extremely high level of satisfaction with respect to the impact of public financing on the firm as a whole.

6.4 Significant differences in the use of public financing and general satisfaction among SMBs in Quebec and in the rest of Canada

An examination of the relevance and use of public financing as perceived by entrepreneurs in Quebec and in the rest of Canada shows, as illustrated in Table 6.1 (section 5), show that more firms outside Quebec (20% more) seek larger amounts of public financing, and do not seem to have qualms about paying more if necessary, since their second objective is a higher profile, and not lower costs, as is the case in Quebec.

These differences, and the lower level of concern among entrepreneurs outside Quebec for using public financing as a way of increasing the interest and commitment of their employees, are largely due to the comparatively larger size of firms outside Quebec and the stricter eligibility criteria of the Toronto Stock Exchange, which demand greater maturity and tested management.

It is interesting to note that satisfaction levels with respect to public financing, as shown in Table 6.1 (section 6), are more or less the same in Quebec and in the rest of Canada. Overall, it can be said that entrepreneurs are very satisfied with both the experience and the effects of public financing on the firm as a whole.

6.5 Conclusions

To sum up, 92% of sampled firms in Quebec feel that the QSSP had a definite influence ("average", "considerable" and "very considerable") on their decision to go public. Nevertheless, 48% (18% "certainly" and 31% "possibly") said they would have gone ahead even without the program.

In addition, the Quebec government directly helped only 40% of the 90 public SMBs to offset a large part of the costs related to prospectus preparation. This means that 60% went public without any specific financial help.

Public SMBs in Quebec, and more particularly in the rest of Canada, are motivated primarily by access to as much capital as possible. In Quebec, other major motivating factors are improved status and internal dynamism.

Finally, 77% of firms in both groups would "certainly" decide to go public if they had the opportunity to make their choice over again, and another 19% would "possibly" do so.

To sum up, these figures, together with the results presented in the preceding chapter, show that the public financing experience is highly satisfactory for firms both inside and outside Quebec, from almost all points of view, except with respect to factors over which the chief executive has little or no control, for example fluctuations in the firm's share price, as seen in Chapter 5.

Chapter 7

IMPACT OF THE STOCK MARKET CRASH OF OCTOBER 19, 1987 ON PUBLIC SMBs IN QUEBEC

7.0 Introduction

The analysis in Chapter 5 showed that the impact of public financing was perceived very positively by owner-managers of listed small firms in Quebec in terms of status of the firm, internal management and on the owner-manager. In fact, in the summer of 1987 - before the stock market crash - more than 75% of chief executives of listed firms in Quebec said that if they had the chance to choose again, they would "certainly" opt for public financing, and another 20% said they would "probably" do so. However, as the survey results are based upon the generally favourable stock market environment, it was deemed necessary to evaluate the impact of the crash on the main responses of the original questionnaire. The purpose of this chapter is to report on the results of a follow-up study undertaken after the crash.

This follow-up survey was conducted on the telephone in August 1988, some ten months after the crash, among the chief executives of the 69 public firms that had already taken part in the research, and the 109 private firms that had also filled out the questionnaire and had indicated their eventual intention to go public ("open-private" firms).

In all, 55 of the 69 public firms were contacted (a response rate of nearly 80%); of the others, three had changed status and eleven refused to be interviewed. A total of 80 of the 106 "open-private" firms (a response rate of 76%) agreed to take part in the telephone interview.

The main objectives of this chapter are to describe the results of this telephone survey as they relate to the impact of the stock market crash on three factors: chief executive satisfaction some time after the event, the intention to go ahead with another public stock offering, with reasons, and the perceived benefits by the owner-manager of the QSSP for the firm and for investors.

TABLE 7.1

**IMPACT OF THE STOCK MARKET CRASH OF OCTOBER 19, 1987
ON PUBLIC AND OPEN-PRIVATE SMBs IN QUEBEC**

Enterprise variables Firm's status	TIME		
	Before the crash (October 1987) (%)	A year after crash (August 1988) (%)	A year after crash. leaving aside stock prices (%)
1. Satisfaction with the fact of being a public firm in general			
- Public firms (N=55 out of 69)			
. very satisfied	56.4	21.8	34.0
. satisfied	36.4	50.9	54.7
. indifferent	1.8	5.5	1.9
. dissatisfied	5.5	21.8	9.4
	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>
2. Commitment to a new stock issue			
- Public firms (N=55 out of 69)			
. yes	34.5	16.4	
. no	65.5	83.6	
	<u>100.0</u>	<u>100.0</u>	
3. Commitment to an initial public offering			
- Open-private firms (N=79 out of 106)			
. yes	24.1	61.9	
. no	75.9	38.1	
	<u>100.0</u>	<u>100.0</u>	

TABLE 7.1 (cont'd)

IMPACT OF THE STOCK MARKET CRASH OF OCTOBER 19, 1987
ON PUBLIC AND OPEN-PRIVATE SMBs IN QUEBEC

Enterprise variables Firm's status	TIME		
	Before the crash (October 1987) (%)	A year after crash (August 1988) (%)	A year after crash. leaving aside stock prices (%)
4. Reasons given by public firm for going ahead with a new stock issue after the crash			
- If yes. give reasons (N=9)			
. better source of funding		22.2	
. process already underway		11.1	
. QSSP		0.0	
. current projects require it		44.4	
. other reasons. e.g. proposals for settlement with shareholders		33.3	
5. Reasons given by public firms for not going ahead with a new stock issue after the crash (N=46)			
. unfavourable market conditions		26.1	
. other sources of funding available		4.3	
. no great need for funding		58.7	
. stock prices too low		8.7	
. other reasons		10.9	

TABLE 7.1 (cont'd)

**IMPACT OF THE STOCK MARKET CRASH OF OCTOBER 19, 1987
ON PUBLIC AND OPEN-PRIVATE SMBs IN QUEBEC**

Enterprise variables Firm's status	TIME		
	Before the crash (October 1987)	A year after crash (August 1988)	A year after crash, leaving aside stock prices
	(%)	(%)	(%)
6. Reasons given by Open-private firms for not going public (August 1988)			
- Open-private firms (N=75)			
. satisfied with present funding		26.7	
. size and general situation with respect to public funding		30.7	
. high cost in terms of time and money		12.0	
. insufficient knowledge of stock market		2.7	
. underpricing		17.3	
. wish to keep control		30.7	
. no need to disclose information		13.3	
. other		40.0	

7.1 Satisfaction among public SMBs in Quebec a year after the stock market crash

Table 7.1 (section 1) shows that overall satisfaction dropped from 92.8% in the summer of 1987 to 72.7% in the summer of 1988. The drop is almost entirely accounted for by firms that were "dissatisfied" before the crash. Therefore, although the drop is considerable, it does not seem as significant as it might have done at first glance.

Chief executives were asked to reassess their overall satisfaction with public financing a year after the crash, but leaving aside the drop in their own firm's stock value resulting from the crash. The intention was to see if the crash itself was the main cause of the lower level of satisfaction, or if there were other reasons. Table 6.1 (section 1) shows that more than 88% of listed small firms in Quebec said they were "satisfied" or "very satisfied" with their

experience, even a year after the crash, if the drop in share prices, over which chief executives had absolutely no control, was not considered.

These results therefore confirm the conclusions of Chapter 5, that is, that the use of public financing is perceived to be highly satisfactory and benefitting the firm in many aspects, except in areas over which chief executives have little or no control.

7.2 Commitment to a new stock issue and reasons

Table 7.1 (sections 2 and 3) shows that 34.5% of public firms intended to issue new stock before the crash, compared with only 16.4% afterwards - a real reduction of 18.1%. On the other hand, the number of private firms intending to go public almost tripled, from 24.1% to 61.9%.

The reasons behind the 18% drop in the number of public firms intending to issue new shares seem clear, given the difficult stock market context. The large increase in the number of private firms intending to go public can perhaps be explained by the fact that a good deal of information on public financing suddenly became available as a result of the crash, and even though share prices were extremely low, owner-managers remained optimistic that recovery would occur, and they continued to pursue their goal of going public. These figures tend to support the conclusions previously reached in this research, that is, that overall satisfaction among firms having gone public is very high, and that interest persists, even after the crash, among firms with the potential to do so.

Table 6.1 also sets out the reasons given by public firms for maintaining (section 4) or abandoning (section 5) their intention to issue new stock a year after the crash, together with the reasons given by "open-private" firms for rejecting the idea of going public in August 1988 (section 6).

Only nine out of the 55 chief executives interviewed in August 1988 said they had considered a new stock issue since the crash. The primary reason, for 44% of them, was that the funds generated by the new stock would enable them to complete their current projects (section 4). Interestingly, not one single chief executive wished to use the QSSP. This could be explained by the fact that investors in QSSP firms had become more selective and less numerous in a falling market context, or by the increased difficulty of eventually being able to sell newly issued stocks.

As can be seen in Table 6.1 (section 5), the most frequently mentioned reason for not having considered issuing new stock since the crash was not the unfavourable market conditions, but rather the fact that additional financing was simply not needed.

But why had private firms that had previously expressed their intention to go public not done so a year after the crash? Table 6.1 (section 6) shows that the main reasons were the

size of the firm, the owner's wish to keep control and satisfaction with current financing methods. Astonishingly, perhaps, dissuasive reasons such as underpricing of stock and high costs in terms of time and money were mentioned by only a small proportion of respondents.

7.3 Assessment of the QSSP - a year after the crash

In an effort to assess the relevance of the QSSP in the difficult stock market context of August 1988, a year after the crash, chief executives were asked how they perceived the program (Table 7.2, section 1).

The results show a clear and considerable confidence in the QSSP, even in August 1988, since more than 75% of public firms and 79% of "open-private" firms considered it to be beneficial. As Table 7.2 (section 2) shows, 60% of public firm chief executives felt that it still remained a reliable program for investors.

Finally, Table 7.2 (section 3) shows that, in August 1988, bank loans were considered the most important complementary or alternative source of financing by both public and "open-private" firms.

7.4 Conclusions

This chapter shows that overall satisfaction among public SMBs in Quebec remained very high (more than 80%), even a year after the stock market crash of October 1987. These results confirm the findings of Chapters 5 and 6, which revealed high satisfaction with respect to the impact of public financing on the firm's status, its internal management and the chief executive himself (Chapter 5). The outcome is considered so positive that 78% of new chief executives said they would "certainly" make the same decision if given the opportunity to choose again, and a further 20% said they would "probably" do so (Chapter 6).

Interestingly, while the number of public firms intending to issue new stock dropped in the year following the crash, the number of "open-private" firms intending to go ahead with an initial public offering increased from 24% to 62% in the same period (Table 6.1, section 3). It seems that the information of all kinds that appeared in public media sources about the stock market crash did not dampen their interest; rather, it had the opposite effect, in that, a year later, even more firms were intending to go public when the time was right.

Finally, despite the crash, more than 75% of public and "open-private" firm chief executives believed that the QSSP was still more beneficial than most other government programs for both firms and investors alike.

TABLE 7.2
ASSESSMENT OF QSSP AND USE OF
ALTERNATIVE FUNDING AFTER THE CRASH

Variables	Firm's status	
	Public firms (N=55)	Open-private firms (N=69)
1. In the present context, nearly a year after the stock market crash, how do you assess the QSSP in comparison with other business funding programs?		
. Better	49.1	44.9
. Slightly better	36.4	34.8
. Slightly worse	1.8	8.7
. Worse	12.7	11.6
2. Favourable perception of QSSP for investors		
. yes	63.6	—
. no	36.4	—
3. Funding methods used after the October 1987 crash		
. SPEQ	0	0.9
. SPEQ-employees	0	1.9
. Venture capital corporations	0	2.8
. SDI	0	9.4
. FDBB	1.4	0.9
. Caisse de dépôts et de placements du Québec	1.4	4.7
. Fonds de solidarité - FTQ	0	0.9
. Shareholding by other firms	0	8.5
. Large bank loans	8.7	32.1
. Others	4.3	1.6

Chapter 8

SUMMARY AND CONCLUSION

8.0 Introduction

This research has shown that the stock market is an important and interesting source of financing for small and medium-sized firms in Canada. It has also helped to understand the phenomenon of public financing and to determine how SMBs could be further encouraged to draw on it.

Particular attention was paid to three particular aspects of public financing: the decision, the listing process and the overall impact. As far as the decision is concerned, factors related to the entrepreneur, the firm and the financial environment were studied. They can all affect the decision of a growing SMB's chief executive to go public.

As far as the listing process is concerned, the research examined how much entrepreneurs knew about eligibility conditions and the initial public offering process as a whole. It also tried to determine the experience of the owner-manager during the period between the decision to go public and the time listing took place.

Finally, the impact of going public on the firm's status, its internal management and the entrepreneur was examined.

In addition, the influence of the Quebec Stock Savings Program on the decision by the owner-managers to go public was analysed. Previously, the program had often been perceived as being extremely influential for SMBs and having a significant impact on the general entrepreneurial climate in Quebec in the 1980s. And, since most of the data were gathered before the crash of October 1987, it seemed appropriate to obtain additional data after that date, to assess the impact of the crash and its effects on data gathered previously.

The study is based upon the information obtained through an 18-page questionnaire sent to four populations: 104 SMB owner-managers in Quebec whose firms had been listed on the Montreal Stock Exchange between 1979 and the summer of 1987; 820 entrepreneurs in Quebec whose firms had the potential to go public but who, at the time the research was carried out, still used private financing; 140 owner-managers in the rest of Canada whose firms were listed on the Toronto Stock Exchange at the time the research was carried out; and 1800 entrepreneurs in the rest of Canada whose firms had the potential to go public but who still used private financing.

This research differs significantly from other research on public financing, which has until now been mainly quantitative in nature and has concentrated the cost/benefit ratio of initial public offerings or profitability and stock market performance of firms on the secondary market. Our own research is qualitative in nature and was concerned more with the overall phenomenon of public financing for SMBs, and in particular focussed on three complementary aspects: decisional factors, knowledge of the listing process and the impacts of public financing as perceived by the entrepreneurs.

8.1 Results

The research results are both significant and convincing. As far as decisional factors are concerned, owner-managers of firms in Quebec are considerably younger (43.1 years old on average) and better educated (79.7% have a university degree, 52.5% in management), and had headed their firm for a shorter period (8.3 years on average) than entrepreneurs who intended to go public, but had not yet done so. The latter were, in turn, younger, better educated and had headed their firms for a shorter period than entrepreneurs who had completely rejected the idea of public financing.

In the rest of Canada the same trends were revealed, although entrepreneurs there were slightly older than the Quebec sample. Fewer had university degrees and, overall, they had headed their firms for slightly longer than their Quebec counterparts.

As far as the firm itself is concerned, public firms in Quebec were significantly younger (having existed for an average of 15.6 years) and had more difficulty obtaining debt or equity financing than private firms with stock market aspirations. The latter, in turn, were younger and had more difficulty obtaining debt or equity financing than firms that had completely rejected the idea of public financing.

The same trends were identified in the rest of Canada, although once again, as was the case for the entrepreneurs themselves, these firms were slightly older than Quebec firms. However, they seemed to experience rather less difficulty obtaining debt or equity financing than was the case in Quebec.

The reasons given for considering public financing were more or less the same for both groups, whether or not the firm had already gone public: acquisitions (53.6%), increased working capital (37.7%), an enterprise project (36.2%) or equipment improvements (30.4%).

Outside Quebec, the reasons were slightly different. Entrepreneurs in public firms said they had chosen public financing primarily to increase working capital (47%), to carry out an enterprise project (43%) or because the time seemed to be right (33%). Private firms considering public financing, however, cited acquisitions (60%) or increased working capital (40%) as their main reasons.

As far as the financial environment is concerned, the results for both Quebec and the rest of Canada confirmed that entrepreneurs in public firms were more familiar with the stock exchange listing process as a whole than were their counterparts in private firms considering public financing. The latter were, in turn, better informed than entrepreneurs who had rejected the idea. However, Quebec entrepreneurs seemed less familiar than their counterparts in the rest of Canada with the role of the Securities Commission and the steps to be taken to go public.

These results reveal that, since the decision to go public is based partly on knowledge of eligibility conditions and the listing process, it is vital for stock market organizations to provide more and better information for potentially interested entrepreneurs.

The results also show that, during the pre-listing period, the step that caused the most concern in Quebec (among 50% of all three groups of entrepreneurs) was drawing up the prospectus, followed by the choice of an underwriter and, finally, the difficulty of satisfying Securities Commission requirements.

As far as the post-listing period is concerned, the data show that the firm's new status is very positively perceived by the manager-owner, and the fear of having to share power seems to diminish once the firm is listed. Statistically significant results show that only 10.1% of "public" entrepreneurs in Quebec, and 6.3% of those in the rest of Canada, said they had been worried about losing a considerable amount of power once the firm became listed. These percentages increased to 32.4% for Quebec and 28% for the rest of Canada among firms that wished to go public but that had not yet done so, and to 66% for Quebec and 45% for the other provinces among those that had rejected the idea of public financing.

As far as choosing an underwriter is concerned, entrepreneurs in Quebec based their decision on criteria such as the quality of service, previous success and reputation, whereas entrepreneurs in the rest of Canada seemed to place more importance on previous success, followed by reputation, with quality of service coming only in third place.

In terms of the impact of public financing, analysis revealed that the most striking change, mentioned by more than half the entrepreneurs in Quebec and in the other provinces, was increased visibility and greater recognition for the firm from the business community and the general public. The firm's new image made it easier to obtain additional private capital.

Changes in management were perceived as being the most important; 47% of firms in Quebec and 42% of those in the other provinces experienced changes of this kind, which were felt mainly through firm restructuring and better overall communications.

It is important to note that only 4.8% of entrepreneurs in public firms in the other provinces, and 4.5% in Quebec, thought that the most important changes caused by public financing had come at the level of decision-making. This contradicts the firmly-held belief that listing automatically means loss of control.

Finally, changes affecting the chief executive - perceived as being the most striking by nearly 7% of entrepreneurs in the other provinces and 3.2% of entrepreneurs in Quebec - mainly took the form of a feeling of recognition and professional pride as a result of stock exchange listing. This was particularly the case in Quebec.

Thus, the results of this research show clearly that, independent of the external environment or geographical location of the firm, going public implies significant changes in terms of the status of the firm, on its internal management and on the the chief executive. However, they also contradict some popular beliefs about the possible loss of control. The most important perceived changes affected the firm's status and not the decision-making powers of the entrepreneur. According to the entrepreneurs questioned, the firm's new "public" status meant that its image and management improved, and also that it had greater access to private sources of financing. External and internal communications were also considerably improved. Therefore, any entrepreneur considering going public should bear in mind a new and greater need to communicate information. Other changes included increased administrative responsibilities and managerial functions. There were also important effects on the employees themselves: most of the entrepreneurs had noticed a greater sense of belonging among their employees. The effects on the chief executive himself were perceived as being the least striking. However, the entrepreneurs who took part in the survey said that they had a greater sense of personal pride and enjoyed a new level of personal recognition in their business community.

8.2 Influence of the QSSP

A total of 92% of the firms in the Quebec sample felt that the Quebec Stock Savings Program, of which they had taken advantage, had a considerable impact on their decision to go public. Nevertheless, 48% believed they would have done so anyway, even without the program.

The primary reason given by public firms outside Quebec for going public was to obtain as much capital as possible, whereas in Quebec, improved status for the firm and internal dynamism were mentioned most often as the important reasons for going public.

It should be noted that 77% of firms in Quebec and the other provinces would "certainly" decide to go public if given the opportunity to make their decision over again, and another 19% would "probably" do so.

These high percentages show that the public financing experience was highly satisfactory from all points of view, except in terms of the chief executive's limited or lack of control over such things as fluctuations in the firm's share price.

8.3 The influence of the stock market crash of October 1987 on the research results

Most of the data used in this research were gathered before October 19, 1987 in a bull market. Therefore, to assess the impact of the crash, a telephone survey was carried out among the Quebec sample in August 1988. A total of 55 of the 69 public firms, and 80 of the 106 private firms with stock market aspirations were contacted, giving a response rate of more than 75% in both cases.

The results of the survey showed that, almost a year after the crash, the number of entrepreneurs who were "very satisfied" with their decision to go public had dropped from 56.4% before the crash to 21.8% afterwards, while the number of "satisfied" entrepreneurs had increased from 36.4% to 50.9%. The 20% drop in the number of "very satisfied" pre-crash responses is therefore accounted for by the "satisfied" responses afterwards. Although important, the drop nevertheless seemed to us to be less significant than it might have been. In fact, when asked to answer the same question independent of the reduction in stock prices which affected all listed firms, 88% of entrepreneurs in public firms said they were "satisfied" or "very satisfied", a drop of only 5% compared with pre-crash levels.

Not surprisingly, the crash also reduced from 34% to 16% the number of public firms intending to issue additional shares. However, the number of private firms intending to go public remained high - 62% - even a year after the crash.

Finally, in August 1988, more than 75% of chief executives in public firms or private firms with stock market aspirations in Quebec still felt that the QSSP was beneficial for both firms and investors alike.

8.4 Lessons for entrepreneurs

The research results show that listing implies important changes for both the entrepreneur and the firm.

As far as the entrepreneur as an individual is concerned, chief executives of newly-listed firms experience higher levels of personal pride and professional recognition, as well as improved social status.

Two major changes affect the firm: its image improves, and its access to external debt or equity financing becomes easier. Thus, not only does going public generate an immediate and considerable influx of funds, it also makes subsequent private financing easier.

However, the most important impact affects internal management, mainly with respect to increased external communications, a greater sense of belonging on the part of the employees and an increase in the number of managerial activities in general.

These changes, although invariably perceived as being positive, nevertheless have a cost. The entrepreneur is faced with more administrative tasks, which leaves him less time for his family, and with a more structured managerial environment, which leaves him less time for his employees. There is also the obligation to provide all kinds of information on the firm's development and its priorities to the general public - including competitors. This obligation was perceived as being extremely demanding and costly. There was also frequent dissatisfaction with fluctuations in firm's share price.

Two general conclusions emerge from these results. First, contrary to the popular belief among entrepreneurs in private firms, it was empirically proven, for the first time, that entrepreneurs in public firms maintain control to a large extent over their firm, even after it goes public. And second, the public financing experience is very positively perceived by those who having chosen to take their firm "public".

Many reasons could explain this new perception of public financing on the part of owner-managers. First, especially in Quebec, and, to a lesser extent in the rest of Canada, we are witnessing the birth of a new generation of entrepreneurs - younger, better educated and trained in management, and also more open to team management and power sharing. Consequently, they do not hesitate to call in outside advisers and to bring competent specialists onto their board of directors. These new entrepreneurs seem more confident in their skills, and are therefore less fearful of losing control.

Stock exchange listing means a considerable influx of funds, but this research shows that it brings with it many other benefits too: it encourages the development of a more structured, rational and open internal management system focused more on the medium and long-term; it fosters closer relationships between management and shop-floor; it enables internal and external communications systems to be better structured; and it gives the firm and its leaders greater visibility among public investors and other firms. These benefits, and others mentioned during the research, should be used to guide future policy-making with respect to encouraging the access to external equity financing for SMBs.

8.5 Lessons for policy-makers

Government interest in facilitating access of SMBs to external capital and equity continues to grow. The Government of Quebec's Stock Savings Program and similar programs instituted by various provincial governments are examples of this interest.

Most government initiatives have concentrated on reducing stock exchange listing costs, either through tax benefits or grants. In either case, the starting hypothesis was that entrepreneurs urgently needing capital to ensure their firm's growth but did not usually consider going public because of the high costs involved.

On the other hand, the review of the literature suggested that the main reasons mentioned by entrepreneurs for their lack of interest in public financing were the fear of losing management control of their firm and the fear of having to disclose important information on the firm. The results of this research with respect to each of these points are interesting.

First, more than 50% of entrepreneurs in sampled public firms said they would have gone public even without government help.

Second, the major reason given by entrepreneurs who had chosen not to go public was not the high costs involved, but simply the fact that they did not need extra funding. These two observations tend to contradict the government hypothesis that SMBs reject public financing because of the cost.

Third, no evidence was discovered to support the belief that going public necessarily means losing control. On the contrary, the results showed that less than 2% of entrepreneurs in public firms had experienced a loss of control over the management of their firm as a result of going public.

Fourth, the results concerning disclosure of information were also interesting. All the entrepreneurs questioned agreed that stock exchange listing meant a considerable increase in outward-directed communication. However, nearly 90% felt that this had a positive impact on the firm.

Fifth, as has already been mentioned, going public brings with it other advantages, including easier access to other sources of external financing and improved management.

Finally, while a return on shareholders' investments should be a priority, it also seems important, in our opinion, to consider the other advantages obtained by public firms and their chief executives, as this research has shown conclusively.

To sum up, if the results of the research are considered good indicators of the real impact of public financing on firms going public, governments should pay more attention to the advantages of stock exchange listing, rather than concentrating mainly on efforts to reduce costs and improve the pricing of the initial public offering through tax and grant incentives.

Two possible methods that can be attempted by governments and other bodies (stock exchanges, underwriters, business associations, and chambers of commerce) for increasing SMB interest in the stock market could be: the establishment of information offices on the process and benefits of public financing, and the provision of written and verbal information through conferences or other means that would foster dialogue between experts and chief executives of growing firms looking for capital.

8.6 General implications

Although this research presents an assessment of the chief executives' perception of the impact of public financing on structural, functional and human aspects, it may also be useful to obtain the opinion of managers and employees in the firms concerned to have a complete overall picture of the phenomenon.

It would also be interesting to assess the impact of the internal dynamic on individual satisfaction within the firm, and on the firm's financial performance.

The relevance of the research results also seems to go beyond national boundaries. They may also be useful for countries where capital markets are no more developed than is the case in North America. Parallel studies could confirm this.

Two main trends emerge from the results. First, the decision to go public means not only an immediate capital input for the firm, but also a positive and permanent change in terms of its external and financial environment. Access to public financing also seems to be a first, and important, step in SMB growth and maturity.

Second, the public financing experience is extremely positive for both the firm and the entrepreneur. Although there are some disadvantages - such as lack of control over share prices - these do not affect overall satisfaction. Consequently, if governments wish to improve the financing environment for SMBs, they should perhaps continue to encourage chief executives to go down the road to public financing. The various forms this encouragement should take depend, of course, on the philosophy and taxation policies of the government concerned.

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ENTREPRENEURS AND INITIAL PUBLIC OFFERINGS: Decision – Process – Impact

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and Vijay M. Jog**

**with the collaboration of
Ghislain F. Th  berge**

Small business and public financing: What kind of entrepreneur decides to go public to fund enterprise projects? What impact does stock market listing have on the firms?

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